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NO. 88-643

In The
Supreme Court of the United States
October Term, 1988

ATLANTIC TELE-NETWORK CO.,
a Virgin Islands corporation,

Petitioner,

v.

THE PUBLIC SERVICES COMMISSION OF THE VIRGIN ISLANDS, PATRICK M. RICE, EXECUTIVE DIRECTOR OF THE PUBLIC SERVICES COMMISSION,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITIONER'S SUPPLEMENTAL BRIEF

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PETITIONER'S SUPPLEMENTAL BRIEF

Petitioner, Atlantic Tele-Network Co., respectfully submits to the Court this Supplemental Brief setting forth a Public Services Commission Hearing held October 25, 1988, after the submission of the Petition for a Writ of Certiorari.

STATEMENT OF FACTS

Atlantic Tele-Network Co. ("ATN"), in the United States District Court of the Virgin Islands, moved the summary judgment asking the Court to find that the Public Services Commission ("PSC") Order 22-1987 was not valid since the PSC decision violated the Government in the Sunshine Act, 1 V.I.C. 251 et. seq. Then ATN moved the Court for a stay of PSC proceedings, in particular the PSC hearing scheduled for October 25, 1988, until all matters resolving the case are decided.

PSC Chief Counsel, Maria Tankenson Hodge ("Hodge"), Esq., argued October 24, 1988, that the PSC Order 22-1987 was not final.

District Court Judge O'Brien, citing footnote 3 to the Third Circuit's decision, decided the PSC Order 22-1987 was not final and PSC hearings could proceed.

On October 25, 1988, the PSC held a hearing which concluded that the sale of the Virgin Islands Telephone Corporation stock ("Vitelco Stock") from ITT Corporation ("ITT") to ATN is to be rescinded subject to an order to show cause to ITT and Rural Telephone Finance Corporation ("RTFC").

ATN objected to the hearing because the only notice ATN received merely noted the docket number and failed to notice ATN of what action was contemplated at such meeting. Further, ATN did not receive Mr. Madan's prefiled testimony until six days before the hearing.

Though there was no formal notice to ITT or Coral Communications, Inc. ("CCI") such parties attended the October 25, 1988 PSC hearing. Samuel Sugden, Esq.,

ATN's and Vitelco's attorney until approximately February 1988, attended as CCI's attorney. ATN had no advance notice that ITT or CCI would be in attendance at the PSC hearing.

I.

THE FACADE OF DUE PROCESS

Since the Third Circuit's decision the course of conduct of the PSC has not changed, but merely has become bolder. Except for a few comments, Petitioner feels the record set forth in the appendix speaks for itself.

In reviewing the appendix herein, Petitioner would like the Court to note:

(i) the October 25, 1988, PSC hearing was the first PSC hearing about the acquisition of Vitelco Stock since April 21, 1987;

(ii) the testimony fails to provide any concrete evidence establishing the required nexus between the acquisition, on one hand, and rates and services, on the other hand;

(iii) the record demonstrates that the PSC does not want to review performance during the sixteen months since closing because all evidence would demonstrate that its position during the previous hearings was unfounded;

(iv) the suggestion of bribery on page 43 of the transcript (App. 55-58) is without merit and is absolutely and unequivocally wrong and baseless;

(v) Mr. Sugden, on page 63 of the transcript, is aware of pre-filed testimony that was only made part of the record and not given at the hearing; and

(vi) Mr. Sugden, on page 64, acknowledges that a rate decrease is proper "because of the 1986 Tax Act." This decrease is at a maximum $300,000 far less than $4.2 million facing Vitelco if ATN retains ownership.

The PSC is clearly treating PSC Order 22-1987 as final because the violation of the Order serves as the only basis to invoke rescission. Without giving ATN a right to contest PSC Order 22-1987 or to contest or comply with any new order the PSC may issue, rescission has been ordered. The PSC looks favorably upon an offer to pay $11.6 million for ATN's stock and assume all debt even though the PSC contended ATN's acquisition price was too high and the debt levels were unacceptable.

PSC counsel, Maria Hodge, Esq., suggests in Respondents' brief in opposition that the Third Circuit's decision should be narrowly construed. In fact, as the attached proceedings illustrate, the Third Circuit decision is broadly construed by the PSC.

The Third Circuit's result oriented decision has been interpreted as a license granting the PSC broad authority to punish ATN for contesting the PSC's jurisdiction.

Respectfully Submitted,

ATLANTIC TELE-NETWORK CO.,
a Virgin Islands corporation,
Petitioner

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EXHIBIT I

VIRGIN ISLANDS
PUBLIC SERVICES COMMISSION
DOCKET NO. 301

IN THE MATTER OF THE SALE OF
VIRGIN ISLANDS TELEPHONE CORPORATION
STOCK TO ATLANTIC TELE-NETWORK CO.

TESTIMONY OF STAFF WITNESS
JAMSHED K. MADAN

OCTOBER, 1988

VIRGIN ISLANDS TELEPHONE CORPORATION
DOCKET NO. 301
TESTIMONY OF JAMSHED K. MADAN

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I. SCOPE AND PURPOSE OF TESTIMONY

Q. Please state your name and address.

A. My name is Jamshed K. Madan, and my business address is 456 Main Street, Ridgefield, Connecticut 06877.

Q. Are you the same Jamshed K. Madan that testified previously in Docket 301 before the PSC?

A. Yes, I am.

Q. What is the scope and purpose of your testimony in this proceeding?

A. It is my understanding from Counsel that the PSC's investigation concerning the sale of VITELCO stock from ITT to ATN has been remanded to the Commission from the District Court based upon the decision reached by the Third Circuit Court of Appeals. Specifically, in an opinion filed on March 10, 1988, the Third Circuit Court of Appeals stated:

> "We hold that the PSC had authority under the pre-amendment statute to impose conditions on the sale of VITELCO's stock as a means of assuring VITELCO's continuing ability to provide adequate facilities and service at reasonable rates. In light of this holding, we need not decide whether the application of the statutory amendment to this sale would violate the contract clause. We will reverse the judgment of the District Court and remand for further proceedings consistent with this opinion."

This Commission has issued several orders with regard to conditions on the proposed sale of VITELCO stock to ATN. In the time following the issuance of the PSC's orders, VITELCO and ATN have undertaken various

transactions and commitments resulting in a changed financial and operating condition for VITELCO. The scope and purpose of my testimony in this proceeding is to provide for the Commission an analysis of the impact of updated information and actions taken by VITELCO and ATN as they reflect upon the conditions imposed by the PSC originally for the proposed sale of VITELCO stock to ATN and, based upon this analysis, to present items for the consideration of the PSC.

II. INTRODUCTION AND PROCEDURAL BACKGROUND

Q. Please provide a brief recap of the orders issued by the PSC relevant to the proposed sale of VITELCO stock to ATN?

A. There have been several orders and actions taken by the PSC with regard to the proposed sale of VITELCO stock to ATN. Specifically:

1. On January 13, 1987, the PSC issued Order No. 1-1987 requesting VITELCO to provide details of the proposed sale of VITELCO stock to ATN.

2. On February 5, 1987, the PSC issued Order No. 3-1987 indicating, amongst other things, that the proposed sale of VITELCO stock to ATN was not to be consummated under the proposed terms and conditions of the sale as described by ATN.

3. On February 25, 1987, the PSC issued Order No. 7-1987 whereby the Commission stated that provided certain changes in the proposed terms of the purchase were implemented, the PSC would con-

sider its original Order prohibiting the sale of VITELCO stock to ATN to be vacated. Order 7-1987 spelled out in detail the changes required in the proposed financing that was to be pursued by ATN to consummate the purchase of VITELCO stock.

4. On April 23, 1987, the PSC issued Order No. 22-1987. In this Order, the PSC recognized that the individuals originally identified as being owners of ATN had changed and that new owners of ATN were committed to pursuing the purchase of VITELCO stock from ITT. The new ownership of ATN was identified as Jeffrey Prosser (27.5%), Cornelius Pryor (27.5%), and E. F. Hutton (45%). In this Order, the PSC included several ordering clauses that were intended to protect VITELCO assets and VITELCO from certain conditions that the PSC determined would not be in the best interest of providing safe and adequate service. Specifically, the PSC Order prohibited any negative pledge on the assets of VITELCO, indicated that the proposed purchasers could not impose a dividend policy that would be adverse to VITELCO, indicated that the proposed sale could not be consummated with the use of a holding company, and required certain guarantees such as the submission of a irrevocable letter of credit, or fully equivalent guarantee on the part of E. F. Hutton in the sum of $15 million.

Subsequent to the PSC's issuance of Order No. 22-1987, on April 23, 1987, VITELCO and ATN sought relief

from the District Court with regard to the Commission's actions on conditions surrounding the proposed sale of VITELCO stock to ATN. On July 7, 1987, the District Court issued an Order in indicating that the PSC, prior to May 19, 1987, was not empowered to grant or withhold approval of the sale of stock of VITELCO to ATN, nor could it impose any conditions on such a sale. In addition, the District Court stated that Act No. 5258 of the Legislature of the Virgin Islands constituted a substantial and unjustified impairment of ATN's legitimate rights and expectations and could not be constitutionally applied to the purchase of VITELCO stock.

Finally, as indicated in the prior section of my testimony, in an Opinion filed on March 10, 1988, the Third Circuit Court of Appeals reversed the Decision of the District Court with regard to the PSC's powers surrounding the sale of VITELCO stock to ATN.

Q. Do you have any observations with regard to developments subsequent to PSC Order No. 22-1987?

A. Since the time that VITELCO received its initial Order from the District Court, it consummated, in its view, the proposed acquisition of VITELCO stock from ATN. In consummating the purchase, VITELCO has clearly violated almost every condition set down by the PSC in its Order No. 22-1987 because VITELCO believed that the PSC Order was not valid. However, even after ATN and VITELCO had received an adverse decision from the Third Circuit Court of Appeals, they continued to pursue policies contrary to the PSC's rulings by forming subsidiaries, paying dividends, etc.

In addition to violating almost every condition which was described in Order No. 22-1987, several additional facts became available with the passage of time, such as the consummation of certain financing by VITELCO and ATN to pay for the purchase of VITELCO stock from ITT. Certainly, since this financing was not underway at the time the Commission undertook its Order No. 22-1987, the Commission had no way of addressing the conditions set forth in the financing documents.

Therefore, I believe it is important for the Commission to understand that, in reviewing the situation, not only are the original facts before the PSC for reconsideration, but, in addition, the details of the financing that were described in great detail in the rate proceeding should also be discussed. As I discussed in Dockets 314 and 316, the restrictions that have been placed upon VITELCO through the financing that has taken place are onerous and not in the best interests of VITELCO in providing safe and adequate service to its ratepayers.

As a result of the hearings in Docket 316, the PSC, on October 11, 1988, issued Order No. 28-1988, where it stated and ordered that VITELCO not transfer, convey, sell, assign, lend or encumber to ATN, VITELCOM, or any person or entity owned by or affiliated with ATN or VITELCOM, any assets of VITELCO without the prior approval of the PSC. The PSC further ordered that VITELCO be restrained and enjoined from declaring and/or paying any dividends or advisory fees to Atlantic or anyone affiliated with Atlantic. Finally, the PSC ordered that VITELCO an ATN notify the PSC in advance in the event of a proposed sale of any material interest in ATN or VITELCO and to provide details of any such transaction to the PSC in advance of its consummation.

III. IMPACT OF UPDATED INFORMATION AND ACTIONS TAKEN BY VITELCO AND ATN

Q. In the prior section you stated that after receiving the decision of the district court, VITELCO took certain actions which violated the conditions set forth in Commission Order No. 22-1987. Would you please summarize the actions taken by VITELCO?

A. In summary, VITELCO consummated the alleged purchase of VITELCO stock form ATN and, the following describes areas where the PSC's conditions in Order No. 22-1987 were violated:

1. The sale of VITELCO did take place using the holding company structure. ATN, which is a holding company, became the purchaser of VITELCO stock in direct contradiction to the PSC Order No. 22-1987 and VITELCO became a wholly owned subsidiary of ATN.

2. The alleged purchase of VITELCO stock was consummated without an irrevocable letter of credit, or fully equivalent financial guarantee on the part of E. F. Hutton in the sum of $15 million which was required by the Order.

3. The purchase price of VITELCO stock, as well as fees payable to various related parties for advisory fees, bridge financing, commitment fees, and other associated financing fees were financed by debt upon instructions of ATN in contradiction to the Commission's Order No. 22-1987.

4. Prior commitments and representations made by prior officers, principals, and attorneys of ATN

were not considered binding and were abandoned by ATN and VITELCO. Specifically, VITELCO stated in various rate proceedings that it did not believe any commitments made with regard to employment to be binding upon VITELCO and/or ATN.

5. VITELCO and/or ATN entered into various employment contracts with the principle shareholders of ATN which were not considered to be arms-length and certainly were not the subject of review by the PSC as required in Order No. 22-1987.

Q. In the prior section you also indicated that VITELCO had undertaken new financing which had imposed conditions on VITELCO and/or ATN which were not in the best interests of VITELCO in providing safe and adequate service. Could you please explain?

A. This item has been the subject of my testimony in Docket 316, and my testimony on Pages 69-79 in that proceeding explained these items in detail. However, to summarize:

1. ATN has unconditionally obligated VITELCO to be responsible for $60 million of debt borrowed directly by VITELCO and then remitted, almost in total to ATN as a dividend, and as guarantor for an additional $44.4 million of debt that has been assumed by ATN.

2. For purposes of the loan agreement, VITELCO and ATN are to be viewed as a single entity. Specifically, in Section 1.08, the loan agreement states that from the point of view of the lender,

the debt service coverage for VITELCO and ATN will be calculated on a consolidated basis for ATN and subsidiaries taken as a whole. This means that the additional debt taken on for ATN, as well as any future additional debt that may be taken on from unregulated and unconnected subsidiaries, would impact on VITELCO both now and in the future. Since ATN at the present time has no revenue other than from VITELCO's present and prior telephone operations, its additional debt reduces the combined VITELCO/ATN coverage and could cause VITELCO to be in a default position.

3. Section 5.03 of the loan agreement indicates that VITELCO is to purchase certain subordinated capital certificates (SCC) in the amount of $10.4 million as a requirement of obtaining the consummated financing. In other words, approximately $10 million of the financing was ascribed entirely to VITELCO to act as a sort of compensating balance to the lender while ATN had no such requirement made of it.

4. Section 6.05 of the loan agreement indicates that the debt service requirement as well as the times interest earned ratio (TIER) is to be considered from a consolidated point of view for ATN and VITELCO taken as a whole. In this section, again, the results of the regulated utility will be impacted by the additional borrowing that has been taken on by ATN and the potential additional borrowing by ATN and other subsidiaries in the future.

5. Section 7.06 of the loan agreement indicates that VITELCO may not take on additional indebtedness other than in a restricted set of circumstances. Here again, ATN has reduced the financial flexibility of VITELCO. It is important for this Commission to bear in mind that prior to the proposed acquisition of VITELCO stock by ATN, VITELCO was debt free and, therefore, possessed great financial flexibility to face the future. By the alleged purchase of VITELCO stock by ATN, all the borrowing capacity of VITELCO has been used to permit VITELCO's new owners to finance its acquisition without making any personal guarantees to finance the transaction and without any compensation or consideration to VITELCO.

6. Section 9.01 of the loan agreement deals with the rights and remedies of the lender of financing to ATN and VITELCO. This section indicates that if there is a particular problem with ATN, that is not related to the operations of VITELCO, VITELCO will also be dragged into a financial default arising out of ATN. This clearly has negative connotations for VITELCO.

7. Section 3.15 of the mortgage and security agreement indicates that any change in the chief operating officer of chief executive officer of VITELCO or ATN must be approved by the lending financial institution. As indicated in my prior testimony, this is an inappropriate condition to be imposed on VITELCO.

Q. What conclusion do you draw from the above?

A. The conclusion I draw is that conditions have changed sufficiently from the time the Commission issued its prior decision in Order No. 22-1987 because the facts surrounding VITELCO and ATN have changed. These changed circumstances must be taken into consideration by this Commission in determining what course of action is appropriate in the future. At a minimum, the terms of the acquisition are both in violation of Order No. 22-1987 and more detrimental to VITELCO than the original terms proposed to the Commission.

IV. ITEMS FOR PSC CONSIDERATION

Q. Given the action taken by VITELCO and ATN at this point, could you please indicate what issues should be brought to the PSC's attention with regard to potential conditions on the sale of VITELCO stock to ATN?

A. There are several items that need to be brought to the PSC's attention. I will deal with several of these items below.

1. *Conditions Imposed by Financing and the Amount of Loan*

The overall amount of borrowing against which VITELCO stock has been pledged remains one of the principal problems with this transaction. As described in my testimony in Docket 316, the unconditional pledge of VITELCO to guarantee $44.4 million of borrowing made solely on behalf of ATN is inappropriate. Therefore, if the PSC were to decide that VITELCO stock should not guarantee any more than VITELCO's operations, then the unconditional pledge of VITELCO to guarantee $44.4 million of debt taken on behalf of ATN should be removed.

All further references in the financing agreement to treating ATN and VIITELCO on a consolidated basis with regard to earnings coverage tests as well as times interest earned ratio tests should also be removed and the financing of VITELCO for its public utility operations should in all manner be divorced from any operations of ATN or any potential future subsidiaries.

The requirement of VITELCO to invest in subordinated capital certificates (SCC) should be made in proportion to the overall debt of VITELCO to the total borrowing. In other words, VITELCO should only be required to invest approximately $6 million in SCCs.

The requirement that the lending institution have a final determination on the next chief operating or executive officer of VITELCO should be removed.

The inability of VITELCO to assume additional debt other than in very restricted conditions should also be removed.

Even with the implementation of all the conditions above, VITELCO will still be almost 100% debt financed. VITELCO must realize that this high leverage will be reflected in the setting of its rates.

It has now been almost 16 months since the alleged purchase of VITELCO. The PSC should mandate a reasonable capital structure. I would recommend a minimum lead of equity of 15% of the capital structure by 1988 and 25% by 1989.

2. *Holding Company Structure*

In my opinion, the Commission's original objection to the use of a holding company structure, as contained in Order No. 22-1987, should continue. In the prior order, the Commission stated that no such sale of VITELCO stock shall provide for the use of a holding company structure except in conjunction with an express prohibition upon the holding company's participation in any venture other than ownership and operation of VITELCO.

The issue of the holding company has been problematical in many respects. First, the Company, under the guise of the holding company, has refused to provide information which would have been relevant to the litigation of the rate proceeding. In addition, financial transactions become much more complicated to be monitored and also provide for the Company to enter into deregulated lines of business which could adversely affect the ability of VITELCO to raise capital in the future, by consuming the value of VITELCO's assets as collateral as well as its earnings as a measure of ability to repay debt.

Finally, it is my understanding from Counsel that if additional lines of business are deemed desirable by VITELCO rather than ATN, separate subsidiaries of VITELCO should be formed which would enable the Commission to directly have access to all information and thereby avoid the problem created by having subsidiaries of ATN.

3. *Intercompany Contracts*

The PSC's Order No. 22-1987 dealt with the issue of intercompany contracts and indicated that any proposed

intercompany contract should be executed at arms-length and be subject to close scrutiny by the PSC. I do not believe it is necessary to repeat here the extended testimony in the rate proceeding with regard to the issue of intercompany contracts. Suffice it to say that this Commission decided that the current contract was not executed at arms-length (the contract was signed by Mr. Prosser for both ATN and VITELCO), and in addition, no scrutiny was requested of the PSC. Given ATN's limited experience in telecommunications, the PSC might want to consider a prohibition against such contracts between VITELCO and ATN and to require that VITELCO's telecommunications advisory, when such advice is necessary, be undertaken in the most efficient and economical manner from a party unrelated to ATN possessing the necessary expertise.

4. *Management of VITELCO*

Subsequent to the alleged purchase of VITELCO stock by ATN, the new owners undertook to remove Mr. Basford as president of VITELCO and promptly installed Mr. Pryor as the Chairman of the Board and Mr. Prosser as President of VITELCO. The PSC's decision in the recently concluded rate proceedings indicated that the salaries related to Mr. Pryor and Prosser were not to be permitted as a valid ratemaking expense and that a reasonable amount for an executive based upon the salary of Mr. Basford prior to the alleged consummation of sale be taken into account in setting rates. If the PSC is not convinced with regard to the capability of Mr. Pryor and Mr. Prosser in managing operating telephone company, then a condition with regard to the sale could require that VITELCO directly hire competent top management to run the telephone

company and that Mr. Pryor and Mr. Prosser remain as investors in this operation. I would point out that representations of ATN officials that no lay-offs would be made for a period of three years did not appear to be treated as binding in the case of the employment of Mr. Basford as president of the telephone company.

5. *ATN Representations Made to the Commission*

The language contained in the Commission's original order still appears appropriate. This language was:

> "Any and all representations to this Commission, made by officers, principals or attorneys of ATN, at any time, shall be and hereby are deemed binding upon ATN, notwithstanding changes in ownership subsequent to such representations."

I believe this language speaks for itself, and this item should be given due reconsideration by the PSC.

6. *Other Costs Associated With the Transaction*

Information received from VITELCO in the course of the rate proceeding indicates that one of the costs of the transaction of the proposed sale of VITELCO stock to ATN has resulted in an additional insurance premium that ATN wishes to charge the Virgin Island ratepayers for in the amount of $1 million. Such an increase in cost to the local ratepayers is significant. The PSC has held open the item of the additional insurance costs for future investigation and determination, but in Dockets 314 and 316, did not make a specific adjustment to disallow these costs in the ratemaking process. In the current situation, where the PSC is investigating the appropriateness of the alleged sale of VITELCO stock to ATN, it should also take into

consideration whether a proposed sale should be consummated given evidence that the sale would result in a direct increase in operating costs of $1 million which the buyer of the stock wishes to pass on automatically to the telephone subscribers of the Virgin Islands. The PSC could certainly take the position that any direct costs arising out of the proposed transaction be paid for by the stockholder rather than the ratepayers of the Virgin Islands.

7. *Purchase of Additional Shares*

Mr. Pryor and Mr. Prosser have made it known that they have negotiated an option to buy out the 45% ownership of Shearson Lehman. This buy-out contradicts testimony given to the PSC that originally E.F. Hutton and then Shearson were in "for the long haul." The financial resources of Shearson were given as major evidence for financial stability of the proposed purchase. Similarly, its experience in and access to expertise in telecommunications were emphasized. Without Shearson, it is not clear what financial resources back the transaction or what access to expertise is provided. As such, the PSC might want to consider the wisdom of releasing the major investor that was presented as having the capability of providing financial resources and services as well as the wisdom of permitting Messrs. Pryor and Prosser from exercising the option to acquire the remaining 45% of VITELCO for themselves.

Q. Are there any other issues which you wish to bring to the attention of this Commission?

A. Yes, there are. During the course of hearings related to proposed legislation for "rate stability",

VITELCO made it clear that it was prepared to undertake certain programs in conjunction with "rate stabilization" which it appeared not to be willing to do with regard to its normal operations. Specifically, VITELCO offered to implement a "911" emergency system and a lifeline plan in the context of a rate stabilization plan.

The implementation of an enhanced "911" plan is of the utmost importance to the people of the Virgin Islands. A delay in the implementation of such a system could have the potential of costing lives while VITELCO is arguing about the appropriate mechanism for a rate structure. In my opinion, given that the technology exists for the implementation of an enhanced "911" system, such a system should be deployed without a delay and not held hostage to the intents of the current alleged owners of VITELCO stock. These actions depict the trade-offs that the current owners are willing to make with regard to operating conditions of the telephone company which would bear analysis upon the Commission's decision to determine whether they ought to be afforded the opportunity to own the telephone company.

Similarly, with a lifeline plan, the elderly, indigent, and handicapped in the Virgin Islands would be afforded low cost telephone service. Such programs have been implemented with great frequency in the United States. A docket with regard to a lifeline program has been opened by this Commission for a considerable amount of time, but the alleged new owners of VITELCO have sought to make implementation of this program conditional upon legislative adoption of their desired rate guarantee law. Here again, the delay in implementation of these plans greatly

increase the suffering of a targeted segment of the population which has every right to receive such relief. Again, holding these people hostage to further the personal aims of the current owners of VITELCO is inappropriate.

In the end analysis, the Commission must decide whether the proponent of the request for approval of consummation of the alleged sale of VITELCO stock to ATN is responsible and capable of running and maintaining an operating telephone company with its high technology. The PSC has dealt with the owners of ATN directly in the course of the recent rate proceedings, has observed their actions in regard to financing and involving VITELCO while the injunction was in place, has encountered the apparent lack of experience with regulatory procedures exhibited by ATN officials—now functioning also as VITELCO officials—and now must make its own analysis with regard to whether it is consistent with the continued financial and operational viability of VITELCO to permit the ownership of the telephone company to be transferred to ATN. As mentioned previously, Mr. Pryor and Mr. Prosser have obtained an option to buy out the interest of Shearson Lehman in VITELCO. When these individuals originally came before the Commission, the financial strength of E.F. Hutton originally and Shearson Lehman subsequently was presented as a significant reason as to why the financial stability of VITELCO would continue into the future. At this time, Mr. Pryor and Mr. Prosser have shown no personal substantial net worth to provide confidence that on their resources alone the financial condition of VITELCO would be safe. The "long-term commitment" of E.F. Hutton and Shearson Lehman appear to

be in doubt. The terms of the financing implemented were highly advantageous to ATN but have no apparent attention to the welfare of the utility. Under these circumstances, the risks to this major public utility's health and strength associated with this proposed sale must be considered—at best—substantial.

Q. Mr. Madan, does this conclude your testimony?

A. Yes, it does.

EXHIBIT II

GOVERNMENT OF
THE VIRGIN ISLANDS OF THE UNITED STATES

PUBLIC SERVICES COMMISSION

RECEIVED NOVEMBER 1, 1988
J. J. PROSSER, PRESIDENT

HEARING IN RE
PSC DOCKET NO. 301

TUESDAY, OCTOBER 25, 1988
10:15 A.M. to 12:22 P.M.

MEMBERS PRESENT

GEORGE C. PARROT, CHAIRMAN
ALFRED B. HAYES, VICE CHAIRMAN
ALPHONSE ADAMS, COMMISSIONER
HECTOR L. RIVERA, COMMISSIONER
MADALINE SEWER, COMMISSIONER

STAFF PRESENT

PATRICK RICE, EXECUTIVE DIRECTOR
MARIA TANKENSON HODGE, LEGAL COUNSEL
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(p. 3) The Chairman: Good morning, ladies and gentlemen, I'll like to reconvene the hearing in Docket 301 this morning.

Mrs. Hodge, will you run us up to date on any aspects of this.

Mrs. Hodge: Yes, Mr. Chairman. The proceeding in the District Court in Civil Number 1987/257 continued as of yesterday afternoon. At that time the District Court heard a motion filed by Atlantic Tele-Network Company for a contemporary restraining order and a preliminary injunction to prohibit the Commission from going forward with its hearing today either upon the grounds that ATN had filed a petition for certiorari to the Supreme Court which the District Court shall allow to be acted upon before the Commission went forward with its proceedings or in the alternative on the grounds that there was a legal deficiency which entitled ATN to prevail relating to the contention that when order Number 22-1987 was entered last year that there was a violation of the Sunshine Act.

The District Court Judge heard argument yesterday afternoon in St. Croix and declined to enter any injunction prohibiting you from going forward today. So at the present time, it is legal and proper for the Commission to continue with its hearing in 301 today.

(p. 4) I have just a few moments ago been served or been handed a copy of a motion for postponement of the hearing, apparently filed by VITELCO with the Commission yesterday. Although the certificate of service reflects that it was served on Friday of last week. To the best of my knowledge, that is not correct. It was not

served on me in any case, and Mr. Rice indicates the Commission did not get its copy until yesterday. It will be proper for the Commission to hear from the attorney for—are you representing both VITELCO and ATN today?

Mr. Sheen: Yes, ma'am.

Mrs. Hodge: Okay. The attorney for VITELCO and ATN in support of its motion for postponement before you proceed, and now will be appropriate time. I have only copy of this, which I can hand up to Chair.

The Chairman: All right.

Mr. Sheen: Mr. Chairman, may I be heard? We filed yesterday with the Commission and with counsel for the Commission a request for a continuance of today's hearing on the grounds that we would like a longer period of time to prepare for a presentation. We don't believe that we had received proper notice of this hearing.

I would like and I respectfully request that the (p. 5) written motion be made a part of this record, and if the hearing is not continued, I'll alternatively request that no decision be taken by the Commission until VITELCO has had an opportunity, VITELCO and ATN, has had an opportunity to address the Commission and respond to any testimony taken today.

The Chairman: Counsel.

Mrs. Hodge: Mr. Chairman, the contents of the motion for continuance in addition to setting forth the positions that were presented to the District Court yesterday takes the position that the notice to the paries represened by Mr. Sheen of your hearing today was not suf-

ficient to give them a reasonable opportunity to prepare. It also takes the position that because the injunction entered by the District Court last year has not been officially vacated by an order of the District Court, that it would be improper for you to go forward. As to the adequacy of the notice, under the provisions of Title 30, section 22, a utility is entitled to ten days notice of a hearing. That notice, I believe, and we may want to check the record to confirm my understanding of this, was served on VITELCO more than ten days prior to today. That is Order Number 29-1988. In as much as the officials of VITELCO and ATN are for the most part the same, I think it will (p. 6) be fair to assume that ATN had notice the same day.

I do not believe that the provisions of Section 22 require you to set forth in text the details of the subject you will take up. Reasonable notice requires that the parties have some idea what you are going to consider, and what they ought to be prepared to address, and the notice did state that it was the intention of the Commission to bring in this matter on for further hearings. PSC Docket Number 301 is one in which the nature of the Commission's investigation has been well known for over a year, and the subject of whether or not the Commission can approve the sale of stock of VITELCO from ITT to ATN, and if so, under what conditions, I think is well established to be the subject of that docket.

In addition, Mr. Madan's testimony was pre-filed last week, so that the utility and ATN had a detailed idea of what Mr. Madan's testimony will be today.

It is my view, therefore, that the notice to the utility and ATN is adequate to go forward today.

I would, however, not anticipate that the Commission would necessarily enter a final order today. It will probably depend on how comfortable you are with the evidence that you hear, and whether you feel there's more matters you want to explore before making a final (p. 7) decision. In particular, since one of the issues before you under the Third Circuit's decision is the possibility of a rescission of this sale, it has been by view that if you determine that that was one of the possibilities that you wanted to keep open after having heard the testimony today, that you probably would want to put ITT on formal notice to come forward and make any showing it felt proper in relation to that remedy. And it also may be proper to give formal notice to the lender, if rescission is one of the options that the Commission is inclined to consider.

So, I wouldn't anticipate that you will necessarily reach a final decision. On the other hand, if Mr. Sheen remarks to the Commission are intended to say that VITELCO and ATN do not consider themselves called upon to provide their position to you today, both in terms of testimony and argument about the details of what their transaction actually included, how they would see them as being consistent with the interest of the utility consumer, I would think that would not be a fair position to take. I think both ATN and VITELCO are on notice to be prepared to make that showing to you today.

So, on the basis of the motion, my advice would be you're not obliged to grant the continuance request, although it is within the Commission discretion to do so.

(p. 8) Mr. Hayes: I'll like to comment, but a question to counsel, too. Wouldn't it be true that if we were to accede to this motion and agree that they didn't have enough information, that it would be a precedent that would prevent anything new coming up at the hearing that hadn't been told to them before. I mean, in other words, it will be a straight jacket that we will be putting the hearing into.

Ms. Hodge: That will probably depend on the basis on which you acted on the motion. If the Commission determined that it will grant the continuance because VITELCO and ATN claimed they didn't have enough notice about what the hearing was about, they might very well set that precedent. If you decided to grant the continuance simply as a courtesy, which you will have the discretion to do, you can do that without setting a precedent.

On the other hand, I would point out to the Commission that the Commission's consultant has not only prepared prefiled testimony, but made the trip to the Virgin Islands to testify today, and the timing of the motion for adjournment is certainly not to be favored while the certificate of service recites it was filed and served on Friday. As I have indicated, the Commission's office didn't receive it until yesterday, the day before (p. 9) the hearing, the day when, of course, Mr. Madan would have had to be travelling, as well as the others who are here today, and I up to and including the today have only seen it handed to me this morning. It has not been served at my office. So, if a continuance was wanted, simply as a courtesy, one might have thought that the motion would

have been filed earlier since the notice of the hearing was served October 13th by hand on VITELCO and there's a substantial period of time thereafter that a motion setting forth these grounds could have been presented.

In any case, it is within the Commission's discretion to grant the continuance or not as it sees fit. I think legally you're entitled to proceed if you choose to do so. And Mr. Madan is available for cross-examination this morning.

Mr. Hayes: We have incurred expenses for this hearing that they appear to be unwilling to contribute to in any way. It is seems to me incredible that they will try to dump onto us some more unnecessary expenses and still try to keep money away from us.

The Chairman: That's my contention also, that we have been put out so many times, and what more information do we need in 301 than what we (p. 10) already have in all of these papers here.

Mr. Hayes: And the other thing is that their rules are— you will remember we asked them early on for a ten day— waiver of a ten day period and they wouldn't consider it. And for no reason except that they wouldn't consider it.

We have got many reasons for turning ths down. And the only reason for accepting it would be, it seems to me, would be a courtesy to them. And I think that that is entirely outside the—outside the necessary or proper action at this time.

The Chairman: Mr. Adams.

Mr. Adams: I just got this and I was reading it. And I note that the scheduled hearings are improper and premature. I think the premature part of it was just really addressed in as far as the timing of the court is concerned; I can't consider it premature. I don't know what the arguments on the impropriety of it are, because it seems to me that we have been and we still are in accordance with law and the order of the Third Circuit Court. So I'll like to know on what grounds they consider the hearings improper.

The Chairman: You want to address that to Mr. Sheen.

Mr. Sheen: Mr. Adams, (p. 11) I'll like to stand on the petition as it has been written. I'll like to have the Commission's permission to have that written statement made a part of the record.

Do I have your permission, Mr. Chairman, to supply to the Court Reporter a copy of the written request for a postponement.

The Chairman: Mrs. Hodge.

Mrs. Hodge: Mr. Adams, if I may briefly address you. As I understand the position in the motion concerning the impropriety the basic contention is that the District Court having entered an injunction prohibiting the Commission from going forward with the impostion of conditions on the sale of stock. Even though the Third though the Third Circuit has reversed that judgment and remanded the matter for further proceedings consistent with its opinion, that strictly speaking the District Court has not entered an order vacating its own injunction which

the Circuit has held erroneous. And the contention perceives that since ATN has filed a petition for certiorari to the Supreme Court essentially it would be inappropriate, unbecoming for the Commission to go forward now when the District Court's injunction has not been vacated by a separate order of the District Court.

However, what I think is disturbing about that is as you will remember since you were in court last week when (p. 12) the Commisison brought on a motion for preliminary inunction to restrain VITELCO and Atlantic Tele-Network from conveying away assets until the matter returned to you for further proceeding, the District Court Judge inquired at that time of Paul Berman of Covington & Burling who appeared on behalf of ATN whether they will stand on the formality that the District Court had not entered an order vacating its own injunction and contend that the Commission could not go forward until such an order was entered and at that time Mr. Berman stated to the Judge of the District Court that they will not rely on such a technicality.

It was my impression at that time that the reason for that exchange between the court and counsel was that we had said the Commission wanted to be particularly certain that it was respectful of the District Court's orders and that it not go forward until the District Court had entered its own order vacating the injunction even if that was in a sense a formality; and that we wanted the District Court's assistance in entering an injunction to protect against transfer of assets until that occurred, until the Commission could resume its own proceedings.

And the District Court Judge at that time was expressing reservation about whether the Commission (p. 13) needed to await any further order of the Court. Essentially it was taking the view that you were free to proceed now. And the question to counsel for ATN at that time was specifically to determine whether that technicality was something they will rely on. The inference I thought was that if they were going to rely on that the District Court might well consider entering an injunction against transfer of assets. And with the assurance of Mr. Berman that they will not rely on that technicality the District Court proceeded to dispose of the motion.

To the best of my recollection, both Mr. Prior and Mr. Prosser was in court when Mr. Berman made that representation that they will not rely on that technicality.

I have a understanding of the fact that Mr. Sheen—when you're co-counsel you can not determine everything about how legal proceedings are done. I think he is within his rights to rely on the wording of the motion.

My own advice to the Commission would be on the basis of those proceedings in District Court at the present time. The contention that it is improper for the Commission to go forward today is not persuasive and that you will be justified in going ahead.

And I think that the proceedings in front of the (p. 14) District Court yesterday are consistent with that. He specifically refused to enter an injunction to stop you from going ahead today. So whatever was to be argued in terms of impropriety of the Commission going forward, evidently was not sufficient to persuade the District Court that you shouldn't continue.

Mr. Sheen: Mr. Parrot, excuse me, may I respectful request a ruling on my request to have the written motion delivered to the court reporter to be incorporated and made a part of this record.

Mrs. Hodge: That's entirely proper, Mr. Chairman.

The Chairman: It shall be.

Mr. Rice: Do you want to give it a number, an exhibit number?

Mr. Sheen: No, sir, I'll just request that the Court Reporter rather than sit here and read the motion, simply have the Court Reporter incorporate it as part of the transcript.

Before The

VIRGIN ISLANDS PUBLIC SERVICES COMMISION
CHARLOTTE AMALIE, ST. THOMAS,
VIRGIN ISLANDS 00801

IN THE MATTER OF THE SALE)	PSC DOCKET
OF (p. 15) STOCK OF THE VIR-)	No. 301
GIN ISLANDS TELEPHONE)	ORDER NO.
CORPORATION)	29/1988

MOTION FOR POSTPONEMENT OF HEARING

The Virgin Islands Telephone Corporation ("Vitelco") and its parent, Atlantic Tele-network Co. (ATN"), hereby urge the Commisison to postpone the hearing in this matter, currently set for October 25, 1988, until the later of (a) the disposition by United States District Court for the Virgin Islands of both pending court cases concerning the Commisison' Order No. 22-1987, in the proceedings; or (b) ten (10) days after the Commission provides adequate notice of the subjects to be covered at the

hearing and the actions, if any, that the Commission proposes to take, as required by the United States Constitution and Virgin Islands law.

By Commission Order No. 29-1988 (the "Order"), received by Vitelco on October 13, 1988, further hearing in Docket 301 has been scheduled for October 25th. The Order states that "the Commission requires further testimony and argument before entering a final order . . . . ".

I.

The scheduled hearings are improper and premature. On April 23, 1987, the Commission entered Order No. (p. 16) 22-1987. On June 20, 1987, the Commission was enjoined by the District Court from approving, disapproving or imposing any conditions on the sale of Vitelco's stock to ATN. *ATN V. PSC*, District Court Civil No. 87-257. In lawful reliance on that Order, which the Commission did not seek to stay, ATN consummated its acquisition of Vitelco stock.

While the United States Court of Appeals for the Third Circuit has reversed the District Court's decision, the Third Circuit did not order the injunction dissolved, and ATN has appealed the Third Circuit's decision to the Supreme Court of the United States. The District Court's injunction against the PSC remains in effect. It is improper for the Commisison to act in any way contrary to the Court's still effective injunction.

It is also premature for the Commisison to consider this matter until *both* court cases concerning Order No. 22-1987, are decided. The issue in the first case (Civil

No. 8-257) was whether the PSC had authority to approve, disapprove or condition the sale. In responding to the Third Circuit's mandate, the District Court could well rule in a way that would affect the Commisison's further deliberation on that issue.

In any event, as the Third Circuit explicitly stated, that case did not involve a determination of the (p. 17) reasonableness of the specific conditions the Commission sought to impose in Order No. 22-1987. The District Court has been called upon to make just that determination (among others) in a separate case (Civil No. 87-347), which is a timely appeal from Order No. 22-1987, pursuant to 30 V.I.C. Section 34. The Court's decision in that separate case will plainly affect any further Commission deliberations in this proceeding. Indeed, under the rules of judicial review, the Commission may well be barred from taking any further action on the matter without first seeking permission of the Court to vacate Order No. 22-1987.

II.

The hearings should also be postponed to enable the Commission to provide adequate notice to Vitelco and a meaningful opportunity to prepare for the hearing as required by the Constitution and the Virgin Islands law. Section 22 of Title 30 of the Virgin Islands Code requires the Commission to give no less than ten (10) days notice of a hearing which might provide the basis for action affecting a utilty such as Vitelco. To be sure, Order No. 29-1988, scheduling hearings for October 25th, was received by Vitelco on October 13th. But the Order provides no indication of the topics concerning which the Commission re-

quires further testimony and (p. 18) argument or what action, if any, the Commission proposes to take based on that testimony or argument. The Order thus gives Vitelco no idea how to begin to prepare for the hearing.

The hearing cannot simply be a continuation of the ago. As the Commission itself recently argued to the United States District court for the Virgin Islands, there have been substantial changes in Vitelco's ownership and financing since the Commission last investigated the matter in April of 1987. *EG.*, Answer and Counterclaim of the Public Services Commission of the Virgin Islands, Civil No. 87-257, pp. 11-12. Thus, the facts that gave rise to the Commission's previous orders in this proceeding have changed, and there is no basis for assuming that the Commisison will now act in any particular way in light of the changed facts and circumstances.

Nor does the proposed testimony of Mr. Jameshed K. Madan, provide the needed notice. Mr. Madan's testimony was received by Vitelco on October 19, 1988, only four (4) business days before the hearing. Mr. Madan's testimony does not purport to be adopted by the Commission, and does not and cannot suffice to provide notice of the matters that the Commission proposes to consider or the actions, if any, that it might take as a (p. 19) result of the hearings. Indeed, Mr. Madan's testimony proceeds from the erorneous assumption that the PSC's investigation of the sale of Vitelco stock to ATN has been remanded to the Commission from the District court.

Mr. Madan's testimony also suggests that the Commission may have in mind adducing testimony concerning

whether events that occurred after the consummation of ATN's acquisition of Vitelco's stock should provide the basis for new or different conditions on Vitelco's relationship to ATN and its shareholders and to Vitelco's and ATN's debtholder. If this is what the Commission in fact intends, then the minimum ten (10) day notice required by 30 V.I.C. Section 22 is wholly inadequate to permit Vitelco to prepare for such a substantial undertaking involving significant matters and considerations that have, to this date, not been heard by the Commission.

WHEREFORE, for the foregoing reasons, the Commission should postpone the hearing scheduled for October 25th, until the late of (a) the disposition by the District Court of both pending cases concerning the Commission's Order No. 22-1987; or (b) a reasonable period after the Commission provides adequate notice of the subjects to be covered at the hearing and the actions, if any, that the Commission proposes to take.

(p. 20) DATED this 21st day of October, 1988.

Respectfully submitted,

VIRGIN ISLANDS TELEPHONE COMPANY
AND
ATLANTIC TELE-NETWORK COMPANY

BY: _____
ALBERT A. SHEEN, OF COUNSEL"

Mr. Hayes: One of the things that it seems to me that I heard in court yesterday from Judge O'Brien was that, that he judged these argument basically that are in this motion and that they are not valid. Were they valid we wouldn't be here this morning, he would have

issued a restraining order. And, it seems clear to me from my recollection of what happened and what he said was that if we were to accept this argument at this time that we are overruling what the Distrit Court Judge just said as recently as 24 hours ago. If not overruling it, ignoring it at our own peril. And it seems to me that there isn't any question of the reasonableness of us proceeding with this hearing at this time and I so move.

Mr. Adams: I second that motion.

(p. 21) The Chairman: It has been moved and it has been seconded. All in favor?

(Show of hands.)

(Unanimous)

The Chairman: The motion is carried and we will continue our hearing in Docket 301 as of this date.

Mrs. Hodge: Mr. Chairman, my view is that the most expeditious way to proceed is to call Mr. Madan who has done some analysis for you of what appears to be the contents of the transaction; and if we can call him now we can present his direct testimony officially.

The Chairman: Mr. Madan. Mr. Dorsett, will you please swear in Mr. Madan.

THEREUPON,

Jamshed K. Madan, being first duly sworn and testified as follows:

(Examination By Mrs. Hodge:)

Q. Will you state your full name for us, please.

A. My name is Jamshed K. Madan. My business address is 456 Main Street, Richfield, Connecticut.

Q. Mr. Madan, on behalf of the Public Services Commission have you prepared pre-filed testimony (p. 22) analyzing the terms of a purported sale of the stock of VITELCO by ITT to ATN?

A. Yes, I have.

Mr. Hodge: Mr. Chairman, may we assign an exhibit number to a copy of Mr. Madan's testimony for the record.

The Chairman: RC-1.

Mr. Rice: Mr. Chairman, we already—the latest one I can lay my hand on is RC-6. So this will be RC-7.

The Chairman: Yes, we pick up from where we left off.

Q. Do you have a copy here before you?

A. Yes, I do.

Q. Do you adopt and ratify this pre-filed testimony as your direct testimony in this phase of these proceedings?

A. Yes, it is.

Mrs. Hodge: Mr. Chairman, may we official make RC-7 a part of the evidenciary record in this docket?

The Chairman: So moved.

Mr. Adams: Second.

The Chairman: All in favor?

(Unanimous)

(p. 23) Mrs. Hodge: Mr. Chairman, I think Mr. Madan can now be made available for cross-examination.

Mr. Sheen: I have no questions of the witness.

The Chairman: Thank you, Mr. Sheen.

The Chairman: Any Commissioners, any questions. Give us a few moments, please.

Mr. Hayes: Mr. Madan, the first question I have is have you ever come to a hearing of a utility and there was no one there to cross-examine you as a witness?

A. No, I haven't, Mr. Chairman. I have had hearings in which attorneys have decided not to cross-examine me before, if that's your question. I believe Mr. Sheen said that he didn't have any questions. There has been other proceedings in which for whatever reasons attorneys have not cross-examined my testimony.

Mr. Hayes: I guess I was struck by the peculiarities of the hearing this morning in that VITELCO is represented by an attorney who really hasn't been in the hearings previously, there is this testimony here but nobody is here to ask you any (p. 24) questions about it. And I just wondered if this is anything that ever happened in your experience before?

A. I can't recall whether the exact same circumstances have occurred. Although the circumstance surrounding this proceedings have certainly been unique in my experience over 15, 17 years of regulation.

Mr. Hayes: And speaking of absences, one of the absences that keeps striking me all the way through is the absent of the creditor. In your research here, what

do we know about the people that have loaned them this 104 million dollars?

A. Mr. Chairman, as you recall the Commission basically instructed its rate counsel and staff sometime in the summer to, at the request of Mr. Prior to go ahead and have certain discussions and try and resolve various issues.

As part of those discussions we had requested financing documents. We had also requested access to the lender. Now as has been the trend with a lot of those discussions they seem to result in an initial contact between the designated representative of VITELCO and ATN with very little feedback and follow on. And with that particular contact, even though we requested a meeting with the Shearson people and the intial indication was that it would perhaps be a good idea, that has never come (p. 25) to pass.

So, for whatever reason, Shearson which owns forty-five percent which is not a controlling interest basically has not been present at these sessions and in addition, at the same initial meetings we requested to meet with the financial people, RTFC, and again for whatever reason that has not come to pass. So I can not comment on it anymore than to simple state the facts that we had requested in effect to meet with them and it was initially thought to be a good idea and it has just never come to pass.

To continue, if the Commission thought it would be useful, I'm not sure exactly what the procedure would be, I'm sure rate counsel will probably be in better posi-

tion to address that, but it perhaps would not be a bad idea to in effect attempt to have the financing people address the Commission at some point.

Mr. Hayes: Well, the question that keeps coming to my mind, early on when the Chicago Bank was involved in this they had three or four people here all the time. When E. F. Hutton was here there were always several of those people. I wasn't thinking of Shearson so much as I was thinking of whatever these other initials are in Nebraska that put up the 104 million dollars.

(p. 26) We have got a docket going on here that it seems to me that could conceivably have some effect on that loan of 104 million dollars and yet I have not seen anybody from that office that has given this money here. And I don't suppose there's anything bad to be drawn from that but, it certainly, it surprises me. I don't understand the vacuum of interest here.

In my business experience I have never known a creditor to loan money and not be interested in what is happening to the money or what the debtor is doing with it and in this case whatever information the creditor has here has got to be secondhand because there has been no firsthand information from the Commission or even this area as far as we can tell.

A. Mr. Chairman, we have obviously a confused situation here as to what the appropriate jurisdiction of this Commission is. I believe ATN and VITELCO think it is one thing and perhaps the Commission will think it different. You're going into a question of strategy which quite frankly I don't feel competent to testify on as to

why they are doing it. It is simply a decision that Mr. Prior and Mr. Prosser seems to collectively have made.

I can tell you that in other proceeding in which the financing is critical, I can think of one offhand which (p. 27) would be as very well kind of publicized one which you probably heard of with the accident at Three-Mile Island. When we were testifying on that and determining what the rate consequences of that incident was, a group of banks that provided the revolving credit agreement were regular participants before the Commission in those proceedings. The information was critical in terms of the future status and certainly if they choose to testify we would sit and listen to what they had to say.

It is really up to them to decide whether they choose to come before you and they will have the burden or presenting whatever evidence they thought was appropriate at this time.

But we do have the financing documents. I have covered in my testimony what some of the conditions that are contained in those documents that are very substantially different to your initial order setting down conditions which is I think one of the key points we are making in this proceeding is that things are very very different to the time that a lot of the initial attempts in this docket were made. There was testimony taken, there was certain negotiations tried early on and this financing came to light well beyond early representations made by VITELCO and ATN.

What I have attempted to do in this testimony is to (p. 28) highlight for you which I'm sure you're well

aware of, a lot of the differences that have occurred. The assumption of debt, the assumption of the guarantee, the combining of the coverage ratios for ATN and VITELCO in total which I believe are very detrimental. In other words, even though you can have a healthy VITELCO you can well have a unhealthy ATN and we have of course seen representations by Mr. Prior on the stand that when that situation occurs protection of ATN seems to be as important a consideration for example as employment. And those are the kinds of things that I have been trying to point out to you.

So, what I have done in my testimony is point those things out. We do have the documents. We know what they say and I have made a series of recommendations as to which particular clauses, which particular important clauses amongst those documents ought to be amended.

If it was your pleasure to consider alternate of conditions which I understand is only one of the avenues open to you, my understanding from counsel is that the Commission has broad discretion based on the Third Circuit decision. There's a wide range of options which this Commission can follow. They are stated very clearly in a footnote in that decision and I'm not prejudging which particular option you all will choose, that's (p. 29) clearly your function, that's up to the Commission.

What I have laid out are the conditions in certain of these financing documents which I believe at an absolute minimum need to be addressed. If that is the route you choose. If you choose other routes the whole question of conditions become moot.

Mr. Hayes: My question wasn't to elicit from you any judgment of strategies on their behalf. It was more to, I have a feeling that the actions of this whole thing, the loan and that sort of thing that there has been nobody here to explain it to us or to—except as done by Mr. Prior and he gave us some explanations that I thought were peculiar when there's a—and one of the peculiar ones as I recall was limit on interest of 10 percent, that said there was a ceiling of ten percent but he testified that that didn't mean anything.

And so, I just wondered if am I unusually apprehensive on this thing or is this a common way for people who loan money not to appear to explain anything?

A. I'm not sure there's anything I would characterize as a common way. Each case has its own circumstances and again not to avoid the question, I certainly think it might have been helpful if ATN and VITELCO and the lender chose to come.

(p. 30) Again, I'm not that familiar with the exact procedural details in terms of if the lender itself could initiate an appearance before this Commission without in effect having VITELCO sponsor that particular party as an individual. It might be an interested party and if it chose it could then appear by itself which has happened in certain proceedings which I'm familiar with. I have seen the whole broad spectrum and it certainly would not have been unusual and I'm sure the Commission would have welcomed their testimony.

It was not available other than through VITELCO and the actual loan documents for which they speak. I

have seen references by certain members in the press when they have board meetings. I believe one of the members of RTFC either sits on either the ATN board or VI-TELCO board and has suggsted publicly in the press that they get together with the Commission. But other than those press releases I can certainly say from a staff standpoint nobody has contacted staff to make any such presentation.

Mr. Hayes: Well, it is clear from your testimony and other things that we know that the situation that exists today is much different from the situation that existed on our April 87 order. And that the order that we put out at that time is not appropriate or in any significant way to cover the (p. 31) situation.

A. Commissioner Hayes I think that true. If you look at my testimony beginning on page eight; eight and nine basically states those things which I believe were in effect in contradiction to your order number 22-87 specifically number one was the use of the holding company. Number two it was consummated without an irrevocable letter of credit or any equity contribution. Number three was your condition, as you recall, that there were millions of dollars, I can't remember the number, somewhere between 14 and 17 million dollars of fees and other arrangements that had to be paid just to consummate the financing which would be to Mr. Blankeneau (phon), it would be to E. F. Hutton which was a substantial receipt of a lot of those fees. Up in the area of 14 to 16 million dollars.

That there was a very specific section in your order stating that prior commitments made by ATN officers be respected and those were not.

And there was also a requirement that employment contracts and inter-company transactions be scrutinized which they weren't. As you recall Mr. Prosser signed these agreements on behalf of ATN and VITELCO both.

And beginning on page ten are the conditions in the financing and those are basically as you can see there is (p. 32) the first one is where VITELCO was obligated not only for its 60 million dollars of debt but an additional forty-four million dollars of debt which the owners of ATN required VITELCO to guarantee and this was the cause of a lot of concern in the rate proceeding. In other words, this is the area where if VITELCO is healthy and ATN isn't, since ATN owns all of VITELCO and owns all of its management, basically can impose certain conditions that can make it intolerable for VITELCO.

Section 108 of the loan agreement talks about how ATN and VITELCO would join together for purposes, and of course this is the situation that we have been hearing about where if again the situation for VITELCO is okay but for ATN isn't, one hears talk of bankruptcy, et cetera.

Number three, is the question of investment in the lender. There was approximately ten percent of investment required which would be approximately ten point four million dollars. ATN unilaterally decided that this investment come entirely from VITELCO which purchased the ten point four million dollars of what is called the subordinated capital certificates. ATN was required to invest zero. In other words, it was a lopsided arrangement.

Six point zero five of the loan agreement talks (p. 33) about the interest coverage ratios and debt service coverage ratios, again showing that ATN and VITELCO are inextricable linked in their operations and, therefore, you can not have one healthy unit and another unhealthy unit.

Section 706 indicates that VITELCO couldn't take on additional debt other than in very limited circumstances which we did not believe was in the interest of VITELCO.

Section 9.01 of the loan agreement talks about the rights and remedies of the lender saying that if there is a default in either VITELCO or ATN, that in effect the lender can call a default and take certain actions with regard to ownership, et cetera, which we believe were not in the interest of the Virgin Islands.

Section 3.15 of the mortgage and security agreement had this condition whereby future chief executive officers and chief operating officers of VITELCO, a local Virgin Islands operating unit, in other words the chief officer had to be approved by the lender in case there was any change and our recommendation of that was that it was an intolerable condition.

So I think in those pages we list both of what they did in violation of your original order and then all the conditions that they imposed subsequent, that were new and need to be taken into consideration by this (p. 34) Commission in its deliberations.

And basically the last chapter of my testimony deals with the issues that I recommend are before you for con-

sideration. That begins on page 14 of my testimony and basically goes through the end of my testimony.

The first area is the condition that were imposed by the financing in the amount of the loan and I believe you're familiar with that, it is if the amount of the loan is excessive leverage by VITELCO to an intolerable kind position.

The second issue on page 16 was the holding company structure which ATN has been using to say that the Commission has no jurisdiction over certain operations and was specifically prohibited by the Commission in terms of the consummation of the sale originally.

The third broad issue deals with inter-company contracts which has been a problem. As you recall in the rate proceedings ATN took the position that is is entitled to 6 percent of the gross revenue of VITELCO without any particular showing of services or benefits received. In addition, there was the whole question of the rate case expenses and how those were paid, et cetera. Those were all part of this inter-company contract issue.

The fourth question was the management of VITELCO (p. 35) which I believe you all had various evidence on in the rate proceeding showing the average experience of a similar set of independent companies that Mr. Prior identified in his testimony and we called up these companies and presented to you an exhibit showing that each one of these chief executive officers had long extensive experience in operating a public utility. So that was an issue.

There was a specific issue of representations made by ATN to the Commission as you recall that originally in your deliberations the original owners of ATN made certain representations and in my discussions with VITELCO and ATN certain of those representations were disavowed because of the holding that initially the District Court felt the PSC didn't have jurisdiction, therefore, I believe it was VITELCO's position that in effect those original hearings made before you did not even occur.

So these again are the representations. This is a pretty important one as you recall because this deals with the representation originally made to the Commission and Senator Redfield that employment contracts will be kept in place for three years.

And you know, we have had some kind of testimony recently as to Mr. Prior position on the employment (p. 36) situation. And of course we have the fact that Mr. Basford is no longer the chief operating officer, the president of VITELCO.

The other issue is the cost associated with the transaction. There's a philosophical issue as to whether when somebody comes before you to consummate a transaction and as a result of that you have an increase in cost, a substantial increase of one million dollars in terms of insurance costs that this automatically be passed through and that this issue be looked at in the overall context as to whether these insurance costs first of all were appropriate, were treated at arms length and the details behind them be known. And even if they were, whether a party coming in to consume a transaction if it results in substantial additional cost to a telephone company and

a request be made that it be passed on automatically to the ratepayers, as to whether this transaction is in the public good. There is no reason philosophically why the ratepayers of the Virgin Islands should automatically pay one million dollars more in telephone charges because somebody else wants to own the telephone company.

Then there was the question of ownership and the question of additional shares and changes in ownership. I believe that the Commission addressed this recently (p. 37) saying that any change in either ATN or VITELCO or any change in ownership between the Shearson position which we understood for the first time through testimony of Mr. Prior or change in the individual ownership of Mr. Prior and Mr. Prosser would be an issue that the Commisssion needed to be notified on and would require Commission approval.

We then talked about in the remaining portion of my testimony the issues of the emergency system, the life line system which from a staff point of view appears to be no reason in the world why these important, in one of them life saving services should in any way be held hostage to these proceedings. It seems to me that those should proceed, VITELCO made offers in public in the summer that they will be willing to implement the 911 system in the context of rate stability plan. Why is it linked to a rate stability plan when this is a life saving service. I'm not sure.

In addition, the life line plan which I can report to you has been docketed by this Commission. Any number of States—I get industry publications and publications

just every month are updating additional States which have implemented life line. I believe the last count the number is somewhere between twenty and 30 days States have implemented substantial life line programs and to (p. 38) make it very specific these would be be reduced cost telephone service available to a targeted segment, usually the poor, the handicap and the indigent.

In my original testimony in 301 I indicated that very favorable rates perhaps $12.00, perhaps even less than $10.00 could be made available to this very needy group of Virgin Islanders which we attempted to negotiate back in January and again that this issue becomes hostage to this particular situation. There is no conceptual link between the implementation of these very needed programs for the Virgin Islands and the issue that is before you at this time. It seems to me that those issues should proceed immediately. There's no reason in the world to hold those hostage. Nine-one-one is a life saving system, why it is being held back is not at all clear and I believe it should proceed immediately.

As I understand your deliberations as soon as the final order in 316 is issued the Commission will order VITELCO to go ahead and implement these two plans. Until such time we will just have to wait and see.

Mr. Hayes: Mr. Madan, the conditions that were outlined in the original order that had been so cavalierly set aside and changed, I don't think it is a matter of ego with the Commission that we go back and say they have to do this sort of (p. 39) thing, but, it is a, it seems to me, a matter of need for the ratepayer of the Virgin Islands that that type of protection that those various conditions

provided to the local community have to be in place. And I don't mean that we had a cement casting there that had to be followed. But we had a series of protections for the ratepayer and as far as that we can see here they have all been cast aside and the only consideration has been for the people who have bought this company. Their interests are the only ones that appear to be at all important here.

And, I feel that it is incumbent upon the Commission to get back to a situation where the ratepayers of the Virgin Islands has got some protection. I don't think it is of any concern of the Commission who owns the telephone company. What the concern of the Commission is the community and the ratepayers. And this business of someone owning the telephone company and then expecting the ratepayers to buy it for them is entirely wrong.

So, though on paper we have got a number of options here it seems to me that that the actions of the present owners of VITELCO are rapidly narrowing our options and our ability to protect the community. They are going to force us to do something on this or they have forced us to do something on it. That is my feeling. I don't (p. 40) think the status quo can continue and I think the path that we will be forced to take, that is is the offices of ATN that are drawing it for us.

Mrs. Hodge: I don't mean to interrupt if other Commissioners have questions, but I did have one question that I would like to ask Mr. Madan if appropriate at this time, Mr. Chairman.

The Chairman: Yes, sure go ahead.

(By Mrs. Hodge:)

Q. Mr. Madan, in your pre-filed testimony you made reference in your discussion of minimum conditions for improved transactions to your ongoing concerns about a holding company structure involving ATN as a parent of VITELCO if ATN is involved in other transactions particularly where it appears that VITELCO is the only asset of value in the overall structure. There was testimony, if I recall correctly either in Docket 314 or Docket 316 from Mr. Prior to the effect that ATN was looking into the possibility of acquiring a telephone company in Trinidad. If the holding company structure as presented in this transaction were retained and ATN were to acquire it, another major caribbean telephone company like Trinidad as they suggested to the Commission they might be planning to do; and if they did so once again as (p. 41) they did in the case of VITELCO essentially with one hundred percent debt financing, in your opinion would there be any substantial risk to VITELCO in the event that there were for example a natural catastrophy in Trinidad that cause damage to a substantial amount of that?

A. I think there would be. And obviously it will depend on the terms of the agreement and how good the agreement was. A natural catastrophy might even be inadequacy of rates in Trinidad. If all of a sudden you found a telephone operating company with a changed political environment where the telephone company didn't receive as favorable a treatment or wasn't protected as well, in effect depending on the circumstance you would have an even more highly leverage situation where the impact on one island could impact on another.

So not only with a telephone company but any transaction in which ATN is pyramiding more than what it already has which is 104 million dollars debt on a total asset value of approximately 60 million dollars which is already substantially in excess, to go ahead and borrow further on the strength of the U.S. Virgin Islands and VITELCO in particular would be a cause of great concern to this Commission and would need to be looked at very carefully.

(p. 42) That was very very clearly one of the original propositions that was the stumbling block which took ATN to originally seek a ruling from the District Court where it felt that the Commission couldn't impose any conditions and certainly not any unreasonabble ones. And very much the original issue with regard to the holding company was, one was access of information which has been extremely problematical and secondly the issue of ATN to go ahead and pyramid additional debt which is of concern to the Commission and ratepayers of the Virgin Islands and protection of VITELCO assets.

To the extent you create a subsidiary of ATN rather than a subsidiary of VITELCO, ATN takes the position—for example VITELCOM a perfect example, that that subsidiary is not under the jurisdiction of this Commission. Whereas if VITELCOM was a subsidiary of VITELCO, a utility, my understanding from counsel is that access to books and records and information is set forth very clearly in the code and that this Commission would have absolute and complete access to this kind of information.

So, I would state again that there's a series of reasonings, one of which is the financing and the jeopardy an dthe second one is the assets and creation of the subsidiary question which is of great concern with regard to the issue of the holding company. And if ATN (p. 43) is proceeding with financing a telephone company it would seem to me that the order issued by the Commission just very recently should gain us another legal interpretation but a financial interpretation would prohibit any such transaction. I believe that was the financial intent of the Commission's decision. The legal intent I'll leave to rate counsel.

Mrs. Hodge: That is all, Mr. Chairman.

Mr. Adams: Mr. Chairman, may be have a short recess.

The Chairman: At this time, we will recess for 15 minutes.

(Recess)

The Chairman: Back on the record, Do you have anymore questions for Mr. Madan.

Mrs. Hodge: No.

The Chairman: Mr. Madan, I have questions in reference to the property at Havensight. Do you recall the value that was given of that property in the original contract of sale?

The Witness: Mr. Chairman, my recollection is that the testimony was that it had a book value of around one hundred thousand dollars as I recall from memory and

that the last appraisal done a (p. 44) couple years ago was in the million dollars or plus range.

The Chairman: Wasn't that property also mortgaged when they received the loan from RTFC?

The Witness: I believe it was. I believe all properties as a general rule.

The Chairman: All properties they owned outright?

The Witness: Mr. Prior said if anything was missed it would be a miracle. Everything was basically mortgaged that he could think of. That's what his testimony was before the Commission.

The Chairman: And the recent sale of the property was one hundred thousand dollars?

The Witness: No, no, the book value was one hundred thousand dollars. As I understand it, there has been no quote unquote sale. There has been a transfers from VITELCO to VITELCOM. There's some question in my mind as to exactly the validity of that transfer. I believe the Commission has kept open that docket because you all had testimony in the rate proceeding suggesting that some alternative kind of treatment be made and I believe the most recent order (p. 45) prohibits a further sale of the property from VITELCOM to any other third party. That's my understanding of that that order. Again, I'll need a legal interpretation. But that's my understanding of the order.

So, I don't know whether that property is up for sale or not. But my understanding is that the order of the Commission does not basically allow a further sale of that property.

The Chairman: Well, I was at a Rotary meeting one particular day about three or four weeks ago and the question, the new president was introduced as of today he's the president of VITELCOM, a completely new business?

The Witness: Billy Shoddy?

The Chairman: Yes.

The Witness: I think they testified to that extent that they have set up this subsidiary and again that subsidiary of course appears to have been created even after the Third Circuit decision which allowed the Commission to set conditions. Obviously it hadn't been remanded back to the Commission but from a timing standpoint that took place even after the Third Circuit decision. And that subsidiary is in whatever state is is, is considered to be legal or not and I'm no expert on that.

(p. 46) It certainly violates the Commission conditions as to whether it should have been created or not.

The Chairman: The book value when it was transferred was one hundred thousand dollars?

The Witness: That's my understanding, sir.

The Chairman: I think that is rather strange because the property adjacent to it two years ago which was about a quater of the size sold for nine hundred thousand dollars with far less structures on it.

The Witness: Yes.

The Chairman: We hear just rumor to the effect if VITELCO transferred that from one person or another

why would a realtor be involved? I'm not asking for a legal opinion; in general.

The Witness: From a practical standpoint transfers of properties from one subsidiary to another, I, at least from my experience, I have never seen any realtors involved in those types of transactions.

I have been involved in any number of proceeding with the breakup of telephone companies, divestiture for example. I have been involved in other proceedings (p. 47) involving transfer of directory properties from an operating company to another subsidiary and to the best of my recollection as long it is still within the umbrella of the parent there should be no reason for any realtor to be involved. It will make no sense. It is just additional cost without any particular purpose that I can see.

The Chairman: I thought it was rather strange because the realtor that was involved was the wife of Senator Magras and we understand that there was a Commission paid for that transfer. Just rumor, nothing in fact.

The Witness: I have no way of knowing whether that.

The Chairman: I thought maybe you had seen something in checking the records of VITELCO.

The Witness: No, I don't believe we have actually looked into that. I believe rate counsel has been assigned agent to pursue the matter further.

I personally have not come across any formal papers or anything to indicate. We didn't have access to any of that stuff in the rate proceeding.

The Chairman: Yes.

(p. 48) Mr. Hayes: Mr. Madan, in the September 30th Commercial Reporter on St. Croix, there's an item in there that says supplement to mortgage and it is by the V. I. Telephone Corporation and it would look like it is all of VITELCO's property on St. Croix. My question is: are you aware of any change in the mortgage status or what the significant of this would be or is?

The Witness: Mr. Hayes, again we are not in an active information gathering stage at this point. Your orders on 314 and 316 are all but final. So, no, I'm not really—really not aware of that. And I'll have to look at the document and basically be instructed by you to go ahead and talk to VITELCO and pursue whatever information you all sort to gather. I'll be happy to do that but at this time outside of the context of the rate proceeding I don't have any particular authority to look into that other than the general surveillance of the Commission.

Mr. Hayes: That was really my question, I wondered if it had come up in any of your conversations with them?

The Witness: No.

Mr. Hayes: My curiosity is what is still turning in the financial side of this (p. 49) company. This doesn't describe anything except as a supplement to the mortgage and it has no dollar amount?

The Witness: And there are no officers here from ATN or VITELCO to answer that question. But if it is your desire I can certainly with your authority go ahead and pursue that if you wished.

Mr. Hayes: I don't think it need be a specific duty at this time. I would think it would be part of some ongoing investigation as we go through with it. It should come out.

The Chairman: Mr. Adams.

Mr. Adams: Mr. Chairman, my concerns were addressed when I found out that there was a hearing in St. Croix yesterday. I knew of it before and then I heard of the cancellation. I didn't know it was rescheduled and held. So I was kind of surprised this morning when I heard about that. That's why I asked for the break so that I could be briefed on it. Now I'm satisfied.

The Chairman: Good, thank you. Mr. Rivera.

Mr. Rivera: No questions.

Ms. Sewer: No questions.

The Chairman: No further questions. Mr. Sheen.

(p. 50) Mr. Sheen: I have nothing to address, sir.

Mrs. Hodge: That is all we have for Mr. Madan at this time, Mr. Chairman.

I believe that that would represent the staff's analysis of the matters pending before you in Docket 301 and that the next step would be appropriate from a procedural schedule would be to now call on VITELCO and/or ATN to call any witnesses they may wish to offer on this matter.

Mr. Sheen: Mr. Chairman, I respectfully request, as a I have in my motion, that no decision be taken today on what is before the Commission. And further I respectfully request that VITELCO and ATN be given an op-

portunity to make a presentation before this body prior to any decision being taken on Docket 301. Thank you.

Mr. Hayes: Counsel, could you tell us why ATN or VITELCO is not prepared day.

Mr. Sheen: Well, I believe we have outlined that, Mr. Hayes, in our petition or motion for postponement of this hearing. We will like an opportunity to respond to Mr. Madan's testimony. It was received last week. We have not had sufficient opportunity to address it. We would like the Commission (p. 51) to exercise the discretion which it has to extend the time within which you make a decision, to extend the time for the purposes of taking testimony, to extend the time to give VITELCO and ATN an opportunity to present evidence on the matter which is before you today.

Mr. Hayes: Well, I don't quite understand the argument. If when the law was written that there was a reason for putting a 10 day period in there as being a reasonable period why does it suddenly become unreasonable. It was more than 10 days, I think you said 13 or 14 days. It—now it is not reasonable. Should we go back to the legislature and get the law changed to make it some longer period. What is so difficult—is this case unique and particularly difficult?

Mr. Sheen: Mr. Hayes, I guess for a number of reasons it would be improper for me to engage in a legal argument with you as to what steps would be appropriate with respect to the notice requirement as it now stands. I think it will be improper for me to do so for a number of reasons.

I stand on my request and respectfully ask that you act favorable on it.

Mr. Hayes: You give us no reason to act favorable on it. If ten days is what (p. 52) the law allows and the simple statement that it isn't long enough doesn't seem to be a reason to change it. There should be a reason on the table as to why this is unreasonable.

Mrs. Hodge: Mr. Chairman, the only thing I can think of that may be appropriate here is to request that the record reflect that which I believe to be true which is that it appears that there's no one present with Mr. Sheen either as a witness for VITELCO or as a witness for ATN. So that we are not in a position to summon any witness forth to testify for you.

I also would like to note for the record that yesterday afternoon when we were in St. Croix before the District Court in relation to the motion advanced by ATN for a preliminary injunction to postpone this hearing that both Mr. Prosser and Mr. Prior were present for that hearing. So, I'll infer from that, that they are in the territory.

The Commission obviously is in a position to decide the motion for a continuance, it has initially at this hearing once declined to grant the motion. I gather from Mr. Sheen that he wishes to renew the motion. It is appropriate for the Chairman to rule on the renewed request for an adjournment.

If the Chair determines not to grant the adjournment (p. 53) we will also note that present today is Mr. Derrick Samuelson whom I believe is an attorney representing ITT.

I would like the record to reflect that ITT has not officially been served with an order to show cause in this proceeding in relation to whether the Commission may or may not approve the sale. But he is present and may wish to address the Commission on matters relating to this docket.

And also present is Samuel Sugden, whom I believe is here in relation to an item of correspondence which reached the Commission this morning which may be viewed as having some relevance to this docket.

But I'll say that from the point of view of your schedule today that the Commission probably through the Chair should next take up Mr. Sheen's renewed motion for adjournment.

Mr. Adams: Mr. Chairman, I move that the motion for postponement of the hearing as it is stated here be rejected by the Commission.

The Chairman: We have a motion that the postponement be denied. Do we have a second?

Mr. Rivera: I'll second the motion.

The Chairman: We have a (p. 54) second that the postponement be denied. All in favor?

(Chorus of ayes.)

The Chairman: It is carried unanimously.

Okay, Mrs. Hodge.

Mrs. Hodge: Mr. Chairman, having offered VITELCO and ATN an opportunity to call witnesses, having denied the renewed motion for adjournment it will be appropriate for the Chair at this point to conclude the pre-

sentation of testimony by Atlantic and VITELCO and to offer an opportunity, if desired, to counsel for ITT to present any remarks he may wish to address to the Commission.

The Chairman: Thank you. Mr. Sheen.

Mr. Sheen: For ITT.

The Chairman: I'm sorry.

Mrs. Hodge: No, I actually meant the Chair may wish to offer Mr. Sheen one last opportunity to address the Commission.

The Chairman: That's what I thought.

Mrs. Hodge: On behalf of VITELCO and ATN. If he has nothing further to offer on behalf of those parties, it will be appropriate for the (p. 55) Chair to close the record as to their participation and to offer an opportunity, if desired, to the attorney for ITT.

The Chairman: Mr. Sheen.

Mr. Sheen: I have nothing further, Mr. Chairman.

The Chairman: May have a motion to close the record on that?

Mr. Hayes: I so move that the hearing so far as the presentation from the parties previously participating be closed or is closed.

Mr. Adams: Seconded.

The Chairman: It has been seconded. Any discussion? All in favor.

(Chorus of ayes.)

The Chairman: The motion is carried.

(Unanimous.)

The Chairman: Mr. Samuelson.

Mr. Samuelson: I'm Derrick Samuelson with ITT. I hadn't planned to make any statement today. But I would say if the Commission were to go in the direction of a rescission that we would wish to make a formal presentation before there were any (p. 56) decision reached.

Our concern would be that after this length of time since the company was sold to the present owners that there certainly are many changes in the way the company is run, the way it is financed. There are probably a number of operational matters that we will have no reason to be aware of. And, therefore, on technical grounds we will have to investigate exactly what had happened to the company and on what terms we might take it back. Although unwilling basically to take it back.

And I say that because we have largely disbanded our tele-communiccation business. The support system which we used to have in operation in San Juan, Puerto Rico, and in Secaucas, New Jersey have largely disappeared. We have sold other companies generally in tele-communications and we are in process of selling more.

So, when we originally decided to sell this business we were getting out of the telephone business, it was our last telephone company and we are still getting out of other types of tele-communications businesses.

So if we were forced despite our concerns to take the company back and assuming one could technically reach

a conclusion as to what it is worth today we will immediately put it up for resale. Because we have no (p. 57) interest in continuing to own it.

So, those are our thoughts informally expressed to you today and as I said before if the Commission decides to proceed further in this direction or to understand what our detailed concerns might be we will be willing to present them to you in a more formal way.

The Chairman: Thank you, sir.

Mr. Sudgen.

Mr. Sugden: Mr. Chairman, I have here today with Mr. Samuelson on behalf of ITT but also on behalf of another group, an investor group that I believe you perceived a letter from called Coral Communications.

I'm really here as a observer and I want to make it very clear that anything that Coral Communications has to put forward is only in the event the Commission and VITELCO do not satisfy—the conditions are not satisfied. In other words, the letter, Mr. Chairman, which you received came from the president of Coral Communications which included a copy of a written offer which was made to Mr. Prior last week. And which pursuant to your own order the president of Coral Communications thought it was incumbent upon him to let you know.

(p. 58) I'm here to answer any questions that I might be able to.

The Chairman: Thank you, sir. Any questions to Sugden.

Mr. Sugden, are you at liberty to tell us some of the members of your board of directors?

The Witness: Let me tell you about the investor group and it is an investor group. It clearly would not manage the day-to-day operations of the telephone company.

The investor group is as stated in the letter has the financial support of Citicorp. The investor group is composed principally of the owners of a different investor group called Silverscreen. Silverscreen has been in existence for four or five years and has been in the business of raising equity money through limited partnerships, principally for Walt Disney, and in that function has been able in the last, I guess four years to raise approximately one point two billion dollars of equity money for Disneyland.

So these are experienced investors and Mr. Steven Davis is president of Coral Communications is also a part of the investor group. He's a former partner of mine at LeBoeuf Lamb and has elected to leave the law firm and become a businessman.

(p. 59) Mr. Hayes: ITT has asked to be offered the opportunity to present its case in the case or in the situation where we vote for rescission. Coral Communications, I guess—would Coral Communications be presenting anything at that time too?

Mr. Sugden: Surely.

Mr. Hayes: You're working with ATN at this time?

The Witness: Yes, that's correct.

Mr. Hayes: But you also clearly have some affiliation or connection—

The Witness: With ITT, absolutely.

Mr. Hayes: So that Coral Communications really is a bridge between the two of them?

The Witness: Only if ATN is willing.

Mr. Hayes: I see. But were we to proceed through or to continue this hearing to make some partial decision and continue the hearing so that ITT can make the presentation that they have asked for this morning, at that time perhaps we will have a better idea of what Coral Communications—

(p. 60) The Witness: Coral Communications would be delighted to tell you more about itself, more about its intentions. I probably can answer quite a few questions here today. But, to have a representative of Citicorp down here, to demonstrate to you their intentions and to have the principals down here also.

Mr. Hayes: Well, from your background and experience in this, you know what the concerns of the Public Services Commission were?

The Witness: I certainly do.

Mr. Hayes: In this buy out and why the unusual circumstances came about where the Commission would be concerned as to who owned the utility which ordinarily shouldn't be our thing.

So, with your knowledge and background of that, would Coral Communications, whatever finally came out of it, would they satisfy the requirements that the Public Services Commission placed on the original sale of this, that's basically the requirements that the ratepayers—

The Witness: Mr. Hayes, I think so. And I'm quite deliberately not giving you an unqualified yes because frankly I have not been involved with VITELCO since January. I'm not aware of everything (p. 61) that has gone on since then. The kind of conditions that you were talking about before then, yes.

Mr. Hayes: That's what I'm talking about. Because we haven't put any other conditions on since then. It is just as you have seen. Whatever conditions we did place on it have been completely ignored and almost in every case the opposite.

The Witness: I'll say this, that if we were to reach agreement with ATN and we could not satisfy the conditions the Commission had then the transaction would not go through. There's absolutely no intention of trying to do anything that is inconsistent with the conditions which the Commission feels are appropriate at this time.

I'm deeply aware that VITELCO is a regulated company and it must respond to the Commission.

Mr. Hayes: The conditions that the public Service Commission put on this sale or attempted to impose on this sale were only conditions that, in our opinion, would protect the community and the ratepayers here. And we really have no interest as to who owns VITELCO.

So, the individual owners are of no consequence. But we do want assurance that our concerns of financial stability in the future, and that sort of thing will be (p. 62) addressed and that the ratepayers won't be put at risk with hair brain schemes or other island purchases?

The Witness: I understand that.

Mrs. Hodge: I have a couple of questions, if I may, Mr. Chairman.

The Chairman: Yes.

(By Mrs. Hodge:)

Q. Mr. Sugden, given the fact that you have had some working with the Commission in the past including some earlier stages of Commission investigations into VITELCO proposed sale as well as its rate setting, I would assume that the group that you were providing advice to would come into a possible acquisition of this sort with its eyes pretty much wide open. May I ask you, preliminarily and not intending to elicit formal legal commitments, is Coral Communications in its discussions with the owners of ATN generally aware of the fact that the Commission has been interested in seeing that 911 service is offered to the people of the Virgin Islands as soon as possible?

A. Yes.

Q. And also that the Commission is interested in seeing that life line service is made available to needy members of the community as soon as possible?

(p. 63) A. Yes.

Q. Are the investors in Coral Communications generally aware of the fact that the Commission has been interested in insuring that there be stability in employment?

A. Yes.

Q. And I see in the letter you sent the Commission an indication that your major financial partner or a major

financial partner in the transaction is Citicorp, the nation's largest holding bank company. Are your investors and Citicorp aware of the Commission's interest in insuring that VITELCO have a reasonable debt equity ratio?

A. They are very much aware, yes, and the Commission will be well aware of what the equity ratio is going to be prior to the time that any transaction is consummated and if that was satisfactory then so be it. And if it was not it would either be revised or the deal would not be consummated.

I'm also aware of Mr. Madan's suggestion, I believe that 15 percent equity ratio be a minimum at a start. And I believe, although I don't want to commit at this stage, that that probably could be worked out.

Q. You also were involved in an early phase of some Commission review of the telephone companies general (p. 64) rates and will recall that there was a point at which there were discussions about negotiating what I'll for purposes of this proceedings call reasonable rate reductions. Are the principals of Coral Communications aware of the fact that the Commission has been engaged in rate proceedings and is looking into the possibility of rate reductions for the people of the Virgin Islands?

A. They are aware of it. They recognize that principally because of the 1986 Tax Act that rates should be reduced and they understand that and accept it.

Q. I take it from the fact that you supplied the Commission a letter from your client to Mr. Prior and not a response that the group that you are representing is

initiating communications with the present owners of ATN but not reached a stage at which there's a joint proposal that you and ATN would present to the Commission?

A. That's absolutely correct. And I believe the meeting that was had with Mr. Prior on Friday of last week was the second meeting that they have had and it was the first time that a written offer had been conveyed to him.

Q. In your letter to the Commission I also noticed a reference to the fact that if Coral was to make this acquisition it is envisioned that VITELCO's day-to-day operation will be conducted with individuals with (p. 65) experience in running telephone companies, is that a fair description?

A. Absolutely true.

Q. May we ask you to assure the Commission at this time that if your discussions with ATN go forward further and your client and ATN reach a point at which it appears there's a serious prospect for an agreement between you that the Commission be kept advised of that?

A. I think the letter that was sent to the Chairman is evidence of our intention to do that. Of course we intend to keep the Commission aware of each and every step.

Q. Would you be in a position to tell the Commission whether to the best of your knowledge the investors in Coral Communications would generally be agreeable to the concept of the Public Services Commission reviewing and having jurisdiction over the transactions of VITELCO and its parent in their dealings in the Virgin Islands?

A. We expect that, yes. And however the transaction, if it is to happen, however it is constructed I believe, we believe, Coral believes that the Commission has jurisdiction over the entire transaction.

Mrs. Hodge: That's all I (p. 66) have for Sugden, Mr. Chairman.

The Chairman: Mr. Sugden, if this transaction came about, would Mr. Basford be retained as president of VITELCO?

A. Mr. Chairman, I have had no discussions with Mr. Basford. I of course have known Mr. Basford for many years and have great respect for him. And he certainly fulfills the criterior of being an experienced operating telephone man. But I think for me to go any further it would probably be inappropriate at this time.

The Chairman: I think it would be the opinion of this Commission and the people of the Virgin Islands that he be retained. Because he's an excellent person in that position, in my opinion.

Mr. Hayes: I'd just like to say it is awful good to see Mr. Sugden down here again. Though we have argued many times in the past it has always been on—

Mr. Sugden: Always respectful.

Mr. Adams: I'm sure Mr. Sugden will remember that when he came back into the picture at one time I was very happy to see him back. So it is on record where I stand where that's concerned.

Mr. Sugden: Thank you.

(p. 67) The Chairman: I think that speaks for all of us.

Mr. Hayes: That doesn't mean we are going to make it any easier for you?

Mr. Sugden: I don't expect it.

The Chairman: Anything further.

Mrs. Hodge: Mr. Chairman, at this point, I'll suggest that it will be appropriate for the Commission to consider whether it wants to enter any order in this docket, either in response to Mr. Samuelson's request that ITT be given an opportunity to appear before you formally if the Commission's inclination is to pursue the possible remedy of rescission or otherwise to address the merits of the matter before you on the basis of the testimony that you have heard.

The Chairman: Thank you, Mr. Sugden.

Mr. Hayes: I'll make a motion in general terms, that—I'll make a motion that the Public Services Commission order that the sale of VITELCO from ITT to ATN be rescinded but, that we not make that final until we have heard from all parties (p. 68) involved, particularly ITT and ATN so that—perhaps the order should be that it is our intent to rescind it and that we are asking to show cause why we should not.

The exact wording I'll like counsel to give us because I think an order such as that is pretty important that is be worded correctly.

But, I think that perhaps what my motion is, is it the consensus of the Commission. We may have overlooked something.

The Chairman: We have a motion before us, do we have a second to it?

Ms. Sewer: I second it.

Mr. Adams: I would want some discussion.

The Chairman: Discussion.

Mr. Adams: It is my understanding in yesterday's hearing Judge O'Brien indicated that he'll take prompt action to proceed and give the Commission the direction that the Third Circuit court had ordered when it wa remanded back to the District Court.

So, since that is presumably coming up soon, I think we should actually wait and see, get Judge O'Brien's order and then proceed when we receive that.

Mr. Hayes: Is that—

(p. 69) Mrs. Hodge: Are you referring to the order that is contemplated from the District Court that will vacate the injunction officially?

Mr. Adams: Yes.

Mrs. Hodge: I think that order is actually anticipated from Judge Christian. And is anticipated relatively soon. Judge O'Brien gave us to understand that he erpected Judge Christian to enter that order himself and he thought it will be entered soon.

If the substance of your suggestion is that the Commission would want to enter a conditional order and defer its final decision until after that order from the District Court is received I can develop wording to do that. If the gist of your suggestion that you prefer not to take

any action, even conditional action until after that order is actually in hand, then I think probably your correct procedural step today would just be adjournment.

Mr. Adams: I was under the impression that Judge O'Brien made the statement that the order would be coming forthwith, within a very short time.

Mrs. Hodge: He told us that he anticipated Judge Christian would enter his order (p. 70) very soon particularly since it is my understanding that Judge Christian will only be officially sitting for about another week.

So, since he told us that Judge Christian will be entering the order and since the Judge will be on the bench only another week he told us he expected the order would be entered soon. If by any chance Judge Christian is occupied with other matters and does not reach that order within the time remaining of his tenure on the bench then I assume Judge O'Brien will enter the order.

What Judge O'Brien told us that he'll reach promptly is the disposition of another case that is pending which is the appeal, which I think is in relation to the petition to reconsider order 22-1987. But I'm not really sure that that need detain you in relation to this motion.

What that really addresses is a different issue.

Mr. Hayes: I think the purpose of my motion is to let all parties be aware of the Public Services Commission intent and tentative decision on this subject to information that ITT or somebody else could bring to us that we haven't heard before.

We have evidently heard all that ATN is going to give us on this, but ITT has asked us for something (p. 71) more. They may have some other information.

But, it is my feeling that what has developed from the hearings has been a clarification of a situation that is so different from that, that we had anticipated the sale of VITELCO to develop into and a situation where the risk to the local ratepayers in the community is so great as to be unacceptable and that the only people than can straighten this out are the people that got us in the mess, that's the people that originally developed it. That's ATN and ITT has got to get back together and work out a different way of doing this.

And I'm optimistic that there's a way to get through it. This will eventually be a lot better for everyone.

Mr. Adams: I have no further discussion. I'm ready to proceed with the vote.

The Chairman: Mrs. Hodge, you see any problem with Commissioner Hayes—

Mrs. Hodge: Well, if I have understood it correctly the motion essentially is to the effect that the Commission having conducted its hearing and heard all the testimony offered today finds, at least preliminarily on that evidence, that a rescission of the sale is warranted in order to comply with the concerns of the Commission which originally caused the opening of this docket, mainly to insure the (p. 72) financial stability of the utility and its ability to provide reasonable service at reasonable rates to the ratepayers. But that it wishes to give to ITT the requested opportunity to be heard and that the procedure

contemplated is a order to show cause directed to ITT if it has any reason why rescission should not be ordered.

If I understand it correctly there's no procedural problems with an order of that kind.

The Chairman: We have the motion. It has been seconded.

All in favor.

(Chorus of ayes.)

(Unanimous.)

The Chairman: It is carried.

So Mrs. Hodge you will prepare the order for us.

Mrs. Hodge: Yes, Mr. Chairman.

Shall we consider a date for the order to show cause or do you want the Executive Director to fix that subsequently?

Mr. Hayes: The question came up, the other party is ATN. But, it seem to me ATN has given us all the testimony they wanted to in this case.

(p. 73) Mrs. Hodge: You have the right in your discretion to make the order to show cause addressed only to ITT since you have already had a hearing which ATN was given an opportunity to be heard or you have the discretion to make the order to show cause addressable both to ITT and ATN whichever the Commission deems appropriate.

Mr. Hayes: I hesitate to open it up to ATN again. The only people that—because this is incredible. They

have evidently don't want to tell us anything. And I think we will just get ourselves in another legal morass or delaying tactics. The only other people who I'm not clear if we are overlooking is the creditors of ATN, whoever they be.

Mrs. Hodge: There's no question that the lender who has been described to you in rate proceedings has a direct stake in several aspects of this transaction. The fact that they entered into those loan agreements without communication with the PSC and at a time when they were on notice of the fact that there was litigation pending whether the sale was valid may put them in a position in which their rights are somewhat less than they might otherwise be, but it certainly would not be inappropriate if the Commission wanted to do so to also issue the order to show cause to the lender (p. 74) giving it an opportunity to if it chose to exercise it, to appear and be heard in relation to a proposed decision.

Mr. Hayes: My only concern is that anybody who might be hurt with this or affected by it know about it. So if ATN has had their opportunity, so that people maybe affected by it would be ITT and whatever this other acronym is in Nebraska or wherever.

Now, does the show cause require them to respond?

Mrs. Hodge: Yes. It gives them an opportunity to go forward and offer any testimony that is relevant to the issue but essentially it opens it up for their affirmative showing.

Mr. Hayes: But they don't have to respond?

Mrs. Hodge: They don't have to, that is correct.

Mr. Hayes: Then I'll request from the Commission that my motion be modified to include the creditor.

The Chairman: Do I have a second?

Mr. Adams: I second it.

The Chairman: Any (p. 75) discussion. No discussion.

All in favor?

(Chorus of ayes.)
(Unanimous.)

The Chairman: The motion will show that the creditor will be included in our order.

Mrs. Hodge: I had left the question lingering whether the Commission wanted to pick a date now for the order to show cause or wanted the Executive Director to schedule it subsequently.

The Chairman: Would the time frame be the same as far as 10 days is concerned?

Mrs. Hodge: I think actually especially if you're going to give notice to the lender for the first time you might want to allow a little more than ten days to make sure the notice gets to them and so on.

The Chairman: November 21, that is okay with everyone.

The Chairman: Is there anything further on this docket.

Mr. Rice, you have anything to add?

Mr. Rice: No, sir.

The Chairman: Nothing (p. 76) further to add in 301, at this time we will adjourn.

All in favor.

(Chorus of Ayes.)

Certified true and correct.

/s/ Theodore A. Dorsett
THEODORE A. DORSETT, CM

EXHIBIT III

PUBLIC SERVICES COMMISSION
P.O. Box 40
Charlotte Amalio, St. Thomas, V.I. 00801
(809) 776-1291

IN THE MATTER OF THE SALE OF STOCK OF THE VIRGIN ISLANDS TELEPHONE CORPORATION	) PSC DOCKET NO. 301) ORDER NO. 31/1988

The above-captioned matter came on for hearing before the Virgin Islands Public Services Commission (hereinafter "Commission") on October 25, 1988 at 10:00 A.M. Present for the Commission were all regular members of the Commission, the Commission's counsel Maria Tankenson Hodge, the Executive Director, Patrick Rice, and Jamshed Madan of Georgetown Consulting Group. Also present were Albert Sheen, Esquire, counsel for the Virgin Islands Telephone Corporation (hereinafter "Vitelco") and Atlantic Tele-Network Company (hereinafter "ATN"), Derrick Samuelson, Assistant General Counsel for International Telephone and Telegraph Corp. (hereinafter "ITT") and Samuel Sudgen, Esquire, representing ITT and Coral Communications, Inc.

The Commission convened the hearing and heard the direct testimony of Jamshed Madan, together with supplemental questions addressed by members of the Commission. He was then made available for cross-examination to counsel for Vitelco and ATN. After counsel indicated he had no cross-examination for the witness, there was no further testimony on the matter of sale of stock between ITT and ATN offered by the Commission's con-

sultants, and counsel for Vitelco and ATN having indicated he had no testimony to offer, the evidentiary record was ordered closed.

Counsel for ITT then addressed the Commission indicating the desire of ITT to make a formal presentation, if the Commission should determine that rescission of the sale was warranted with particular reference to the need to determine the value of the corporation as it would stand at the time of rescission and other matters of concern to the seller.

Counsel for Coral Communications referred to a letter to the Commission expressing the interest of Coral in acquiring the stock of ATN. Said letter was made a part of the record. Mr. Sugden assurred the Commission that any proposed acquisition of ATN by Coral would be made consistent with the Commission's role as the regulatory body supervising the public utilities in the territory.

On the basis of all the testimony adduced consisting entirely of the testimony of Mr. Madan, which was neither impeached by cross-examination nor contradicted on any point by any other witness, the Commission determined that rescission of the sale of Vitelco stock by ITT to ATN was necessary, inasmuch as the terms on which the transaction had taken place, as described in some detail in the testimony of Mr. Madan and the closing documents submitted to him for review, were inconsistent with the financial stability and integrity of the utility and the ability of the utility on an ongoing basis to provide adequate service at reasonable rates.

In particular, Mr. Madan testified, without contradiction, after analysis of the financing and conduct asso-

ciated with the sale of Vitelco's stock, that the restrictions imposed upon Vitelco through financing were onerous and not in the best interests of Vitelco in providing safe and adequate service to its ratepayers. He further testified as to the aspects of the transaction which were inconsistent with the utility's ability to provide safe and adequate service, including the fact that ATN has unconditionally obligated Vitelco to be responsible for $60 millon dollars of debt, secured by mortgages on all Vitelco real property, and then remitted almost in total to ATN as a dividend. ATN also caused Vitelco to guarantee, without apparent compensation, an additional $44.4 million dollars in debt undertaken by ATN for the purchase, thereby converting Vitelco from an almost 100% equity-financed entity to an almost 100% debt-burdened corporation, solely for the purpose of financing the purchase of stock which had not benefited Vitelco in any respect.

Mr. Madan pointed out a number of covenants in the loan agreement which substantially restrict the ability of Vitelco to conduct its own affairs, to determine its own revenue requirements, to pick its own executives, and to borrow funds if needed for its own purposes, and he concluded on the basis of this detailed analysis that the terms of acquisition actually entered into by ATN, would have been a violation of Order 22/1987 had the court's injunction not been in place; and indeed are *more* detrimental to Vitelco than the original terms of acquisition proposed to the Commission in 1987.

Further, he noted the utility had been caused to enter into a contract with a related party namely, ATN, the new owner, for advisory services, which we have previously

indicated we consider totally inconsistent with Vitelco's welfare, and without any evidence that the six percent (6%) gross revenues paid to ATN produces anything approaching equivalent value. This is particularly objectionable because it is apparent that ATN caused the agreement to be signed on behalf of the utility by an ATN principal without prior Vitelco board review, immediately at the time of closing, and without any identifiable purpose other than to extract large amounts of revenue from the public utility.

Moreover, immediately after closing experienced management was replaced with inexperienced officers whose only qualification for the position was their ownership interest in ATN, clearly a detriment to Vitelco.

The Commission having concluded that all of Mr. Madan's testimony was credible and persuasive, adopts his analysis as the findings of the Commission in addition to the foregoing. Also, we conclude that the terms of Order 22/1987 can have no ongoing application in relation to a transaction which was consummated on terms entirely different from those presented to the Commission at the time of that order, and therefore direct that Order 22/1987 be superceded by this order.

AND IT IS HEREBY FURTHER ORDERED that the sale of stock of the Virgin Islands Telephone Corporation by ITT to ATN shall be rescinded, provided, however, that ITT Corp and Rural Telephone Financing Corporation may show cause, if any there be, on November 21, 1988 at 10:00 A.M., at the Buena Vista Room of the Bluebeards Castle Hotel, why the transaction should not be rescinded, or if rescission proceeds, what terms and con-

ditions would be appropriate to include in a final order to implement such rescission, including without limitation any necessary and appropriate provisions to assure the parties to the transaction that the value of the stock as returned is equal to the value of the stock as conveyed, or to permit the parties an opportunity to verify and confirm the value of the stock as it would be returned and thereby to determine the appropriate sum to be remitted by the seller to the buyer as part of the rescission. Any party proposing to appear and show cause at the hearing above-scheduled shall pre-file, in writing, with the Commission, not less than five (5) days prior thereto, such party's direct testimony, and shall cause of copy thereof to be served upon counsel for the Commission, and all other parties.

In connection with this order of rescission, the Commission further orders that, if an appropriate request to approve another proposed sale of Vitelco's stock by ITT to ATN or any other prospective purchaser is to be presented to the Commission, it shall be submitted with sufficient detail in advance of proposed closing, to permit the proposed terms of sale to be reviewed by the Commission in conformity with the provisions of Title 30 of the Virgin Islands Code.

During the pendency of this order the provisions of Order Nos. 28/1988 and 29/1988 shall be in all respects complied with.

DATED: 11/10/88

/s/ George C. Parrott
GEORGE C. PARROTT, Chairman

Copies sent by Registered Mail and by Telefax transmission to:

Virgin Islands Telephone Corporation (VITELCO)
Atlantic Tele-Network Company (ATN)
International Telephone and Telegraph Corp. (ITT)
Rural Telephone Financing Corp. (RTFC)

EXHIBIT IV

ARTHUR ANDERSEN & CO.

ATLANTIC TELE-NETWORK CO.
(Parent company only)

FINANCIAL STATEMENTS
AS OF DECEMBER 31, 1987
TOGETHER WITH AUDITOR'S REPORT

ARTHUR ANDERSEN & CO.
Chicago, Illinois

To the Board of Directors of

Atlantic Tele-Network Co.:

We have examined the balance sheet of ATLANTIC TELE-NETWORK CO. ("the Company") (parent company only) (a Virgin Islands corporation) as of December 31, 1987, and the related statements of income, retained earnings and cash flows for the period from June 25, 1987 (date of inception), to December 31, 1987. Our examination was made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

As set forth in Note 2 to the financial statements, as a result of a decision of the United States Court of Appeals, the Virgin Islands Public Service Commission could impose various conditions on the Company's continued ownership of Virgin Islands Telephone Corporation. In the opinion of management, any fines or other conditions imposed will not have a material effect on the financial statements.

In our opinion, the financial statements referred to above present fairly the financial position of Atlantic Tele-Network Co. (parent company only) as of December 31, 1987, and the results of its operations and its cash flows for the period from June 25, 1987 (date of inception), to December 31, 1987, in conformity with generally accepted accounting principles.

April 8, 1988

ATLANTIC TELE-NETWORK CO.

(Parent company only)

BALANCE SHEET—DECEMBER 31, 1987

(In thousands)

ASSETS

CURRENT ASSETS:	
Cash	$ 375
Consulting fees receivable	43
Due from subsidiary (Note 3)	1,560
	$ 1,978
FIXED ASSETS:	
Land	$ 124
Investment in subsidiary (Note 3)	49,046
	$49,170
DEFERRED ASSETS (Note 9):	
Debt issuance cost	$ 3,085
Organization costs	455
	$ 3,540
Total assets	$54,688

LIABILITIES AND STOCKHOLDERS' EQUITY	
CURRENT LIABILITIES:	
Current portion of long-term debt	$ 814
Accounts payable	2,360
	$ 3,174
LONG-TERM DEBT (Note 8)	43,630
Total liabilities	$46,804
STOCKHOLDERS' EQUITY:	
Common stock	$ 20
Additional paid-in capital	2,980
Retained earnings	4,884
Total stockholders' equity	$ 7,884
Total liabilities and stockholders' equity	$54,688

The accompanying notes to financial statements are an integral part of this statement.

ATLANTIC TELE-NETWORK CO.

(Parent company only)

STATEMENT OF INCOME
FOR THE PERIOD FROM JUNE 25, 1987
(DATE OF INCEPTION), TO DECEMBER 31, 1987

(In thousands)

REVENUES:	
Advisory fees	$ 1,627
Consulting fees	43
Total revenues	$ 1,670

EXPENSES:	
Legal, consulting and management expense	$ 80
Amortization of organization costs (Note 9)	51
Amortization of excess of purchase price over underlying book value (Note 1)	614
Interest expense, including amortization of debt issuance cost of $235	6,383
Total expenses	$ 7,128
Loss before taxes	$(5,458)
INCOME TAX EFFECT OF PARENT COMPANY OPERATIONS (Note 4)	1,811
Net loss before equity in earnings of subsidiary	$(3,647)
EQUITY IN EARNINGS OF SUBSIDIARY (Note 3)	8,531
NET INCOME	$ 4,884

The accompanying notes to financial statements are an integral part of this statement.

ATLANTIC TELE-NETWORK CO.

(Parent company only)

STATEMENT OF RETAINED EARNINGS FOR THE PERIOD FROM JUNE 25, 1987 (DATE OF INCEPTION), TO DECEMBER 31, 1987

(In thousands)

BALANCE, beginning of period	$ —
Add—Net income	4,884
BALANCE, end of period	$4,884

The accompanying notes to financial statements are an integral part of this statement.

ATLANTIC TELE-NETWORK CO.

(Parent company only)

STATEMENT OF CASH FLOWS
FOR THE PERIOD FROM JUNE 25, 1987 (DATE OF INCEPTION), TO DECEMBER 31, 1987

(In thousands)

CASH FLOWS FROM OPERATING ACTIVITIES:	
Net income	$ 4,884
Add (deduct)—Adjustments to reconcile net income to net cash provided by operating activities—	
Amortization of excess of purchase price over underlying book value	614
Amortization of organization costs	51
Consulting fees receivable	(43)
Due from subsidiary	(1,560)
Accounts payable	2,360
Organization costs	(506)
Deferred debt issuance costs	(3,085)
Net cash flows from operating activities	$ 2,715
CASH FLOWS FROM INVESTING ACTIVITIES:	
Land	$ (124)
Investment in Vitelco	(49,660)
Net cash flows from investing activities	$(49,784)
CASH FLOWS FROM FINANCING ACTIVITIES:	
Issuance of debt	$ 44,444
Issuance of common stock	3,000

Net cash flows from financing activities	$ 47,444
Net increase in cash	$ 375
CASH AT BEGINNING OF PERIOD	—
CASH AT END OF PERIOD	$ 375

The accompanying notes to financial statements are an integral part of this statement.

ATLANTIC TELE-NETWORK CO.

(Parent company only)

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 1987

(1) GENERAL:

Atlantic Tele-Network Co. ("ATN" or the "Company") is a U. S. Virgin Islands corporation formed on June 24, 1987. The Company acquired all of the outstanding common stock of the Virgin Islands Telephone Corporation ("Vitelco") from ITT Communications Services, Inc. ("ITT") effective June 25, 1987, in a business combination accounted for as a purchase. The total cost of the acquisition was $41,298,000, over the underlying book value of Vitelco. Such excess is being amortized on the straight-line method over 35 years.

Vitelco is primarily engaged in providing telecommunications service in the U. S. Virgin Islands.

(2) ACQUISITION LITIGATION:

The purchase referred to in Note 1 is being contested by the Virgin Islands Public Service Commission ("VIPSC").

On April 23, 1987, the VIPSC issued an order disapproving the then-proposed sale of Vitelco's stock from ITT Communications Services, Inc. to ATN unless certain conditions were met. On June 19, 1987, in an action brought by ATN, the United States District Court for the Virgin Islands (the "District Court") held that the VIPSC did not have statutory authority to approve, disapprove or condition the sale of Vitelco's stock. On June 24, 1987, the sale of Vitelco's stock to ATN was consummated without ATN's or Vitelco's complying fully with the conditions in the VIPSC order. The District Court formally entered an injunction prohibiting the VIPSC from interfering with the sale on July 7, 1987.

On March 10, 1988, the United States Court of Appeals for the Third Circuit (the "Third Circuit") handed down a decision reversing the District Court and holding that the VIPSC had statutory authority to impose conditions on the sale of Vitelco's stock. The Court also suggested, but did not hold, that the VIPSC could seek to rescind the sale or impose fines on Vitelco or ATN for consummating the sale in violation of the VIPSC order.

ATN has timely sought rehearing of the Third Circuit's decision, the effect of which is therefore stayed until ATN's rehearing request is determined. If the Third Circuit denies ATN's rehearing request, it is expected that the VIPSC will seek remand of the matter from the District Court to the VIPSC for consideration of the action, if any, that it should take in light of the fact that ATN has consummated its acquisition of Vitelco's stock and has obtained new and different financing, as described in Note 8.

On August 13, 1987, while the above-described action was pending in the Third Circuit, ATN and Vitelco appealed to the District Court for review of the VIPSC order on other grounds. That appeal has been held in abeyance pending the resolution of the Third Circuit as described above. If the Third Circuit does not grant its rehearing petition, ATN intends vigorously to contest the VIPSC order before the District Court.

Under the circumstances, ATN and its attorneys believe it unlikely that VIPSC will require outright rescission of ATN's acquisition of Vitelco's stock. Neither the VIPSC staff nor the VIPSC itself has formally or informally proposed specific fines or conditions or identified what remedies, if any, it will pursue if Vitelco does not comply with any conditions the VIPSC may ultimately impose. However, in the opinion of ATN and its attorneys, any fines imposed would be limited by statute to $100 per day. Furthermore, in the opinion of the Company, other conditions or remedies ultimately specified will not have a material effect on the financial statements.

(3) SIGNIFICANT ACCOUNTING POLICIES:

Basis of Presentation—

The accounting policies of ATN conform to generally accepted accounting principles. The financial statements have been prepared following the equity method of accounting, and, as such, the statement of income reflects the Company's equity in the earnings of Vitelco since the date of acquisition.

Investment in Subsidiary—

ATN's investment in all of the outstanding common stock of Vitelco, based on the equity method of accounting

at December 31, 1987, consists of the following (in thousands):

Paid to ITT Communication Services Inc. for purchase of common stock	$87,428
Acquisition costs	6,686
Distribution from Vitelco	(52,985)
Earnings of Vitelco from date of inception to December 31, 1987	8,531
Amortization of excess of purchase price over underlying book value	(614)
Investment in Vitelco	$49,046

The earnings of Vitelco from date of inception to December 31, 1987, consist of the following (in thousands):

Local telephone service revenues	$ 8,763
Toll service and access charge revenues	16,913
Miscellaneous	2,341
Total operating revenues	$28,017
Depreciation and amortization	$ 3,453
Taxes, other than income taxes	1,341
Other operating expenses	10,797
Other (income) deductions, net	(299)
Total expenses	$15,292
Income before income taxes	$12,725
Income taxes	4,194
Net income	$ 8,531

Revenue of Vitelco—

Vitelco's revenue consists of local service and access charges which are recognized when earned, regardless of the period in which they are billed.

Access charges are billed by Vitelco to the long-distance carriers. These charges are for interconnection with local facilities and for end-user charges to multiline business, single-line business, and residential customers for access to long-distance facilities.

Access revenue are recorded on the basis of estimated allocations of plant and operating expenses to long-distance service. These estimates are subject to review by the National Exchange Carriers Association ("NECA"). The years 1986 and 1987 are still open for such review. The FCC has ruled that the authorized rate of return which exchange carriers (such as Vitelco) may earn for providing interstate access service is 12% for 1987 and 1988. In management's opinion, subsequent adjustments resulting from the NECA review and the FCC limits on the authorized rate of return will not significantly affect the accompanying financial statements.

Due to uncertainties included in the review and settlement process, only a portion of such estimated access revenues is recorded as revenues, and the remainder is recorded as a current liability.

During 1987, subsequent to its acquisition by ATN, Vitelco concluded negotiations with AT&T and NECA with respect to the period 1984 and 1985 and refined its estimates for 1986. As a result, net revenues for such periods were increased in excess of those previously re-

flected in prior years by approximately $7,006,000. This amount has been included in the Company's equity in the earnings of Vitelco on the accompanying financial statements.

(4) TAXES:

ATN and its subsidiary will file tax returns covering the period from inception through December 31, 1987.

Deferred income taxes are provided for timing differences, principally due to the use of accelerated depreciation for income tax purposes. Accumulated deferred taxes are credited to income as the related timing differences reverse.

Investment tax credits related to regulated telephone operations have been deferred and are being amortized to income over the service lives of the related property. Investment tax credits applicable to other operations are used to reduce income tax expense currently, or in the year when such operations are no longer regulated.

Total income tax expense above divided by the sum of such tax expense and net income results in effective income tax rates of 32.8% for the period from June 25, 1987, to December 31, 1987. The following table reconciles the weighted statutory income tax rate (including the 10% Virgin Islands surcharge) to these effective income tax rates:

Statutory income tax rate	37.4%
Amortization of investment tax credit	(9.0)
Amortization of cost in excess of underlying book value not deductible for tax purposes	8.5

Other	(4.1)
Effective income tax rate	32.8%

In December, 1987, the Financial Accounting Standards Board ("FASB") issued Statement No. 96, "Accounting for Income Taxes," which supersedes previous income tax accounting standards and pronouncements. ATN is required to adopt the new accounting and disclosure rules no later than 1989, although earlier implementation is permitted. ATN has no decided when it will adopt the new standard. ATN is currently analyzing the provisions of FASB No. 96 and the effect that the change will have on the ATN's reported consolidated financial position and results of operations.

(5) RETIREMENT PLANS:

Vitelco has computed its pension cost in accordance with Statement of Financial Accounting Standards No. 87, "Employers' Accounting for Pensions."

Vitelco has a noncontributory plan for eligible hourly employees. Net periodic pension cost for the period from inception to December 31, 1987, was (in thousands):

Service cost	$ 44
Interest on projected benefit obligation	45
Actual return on assets	(119)
Net amortization and deferral	64
Net periodic pension cost	$ 34

The following table sets forth the funded status, the amounts recognized in the consolidated balance sheet of

Vitelco at December 31, 1987, and the principal assumptions of Vitelco's plan (in thousands):

Actuarial present value of benefit obligations—	
Vested benefits	$ 970
Nonvested benefits	223
Projected benefit obligation	$1,193
Plan assets at fair market value	1,323
Plan assets in excess of projected obligation	$ 130
Unrecognized net loss	10
Unrecognized prior service cost	103
Unrecognized net asset at January 1, 1987	(267)
Pension liability included in the balance sheet	$ (24)
Weighted average discount rate	8.50%
Expected rate of return on invested assets	9.75%

Until ATN acquired Vitelco in June, Vitelco participated in the ITT Salaried Retirement Plan. Subsequent to the acquisition, Vitelco's salaried employees will be included in the Company's management pension plan. ATN has not yet finalized its management pension plan, but the plan will be structured similar to Vitelco's plan with ITT. ATN's equity in the earnings of Vitelco includes approximately $175,000 of pension expense in the accompanying

financial statements related to the estimated costs of the plan for the period from June 25, 1987, to December 31, 1987.

(6) REGULATORY MATTERS:

In 1987, the VIPSC instituted a surveillance proceeding to determine whether Vitelco was earning in excess of its last allowed rate of return. The VIPSC staff submitted various reports to the VIPSC concluding that Vitelco's 1986 and 1987 earnings on local telephone service exceeded its authorized rate of return and recommending a $1.545 million reduction, based on 1986 earnings, in Vitelco's local telephone rates over a twelve-month period commencing on November 1, 1987. Based on estimated 1987 earnings, the VIPSC staff recommended an immediate rate reduction of up to $2.452 million. Hearings were held between September, 1987, and February, 1988.

Although the VIPSC has not issued any decision with respect to such proceeding, Vitelco believes that it is earning less than its allowed rate of return and, accordingly, no downward adjustment in rates is appropriate. However, the Company cannot predict what the VIPSC decision will be or ascertain at this stage of the proceeding the amount, if any, or the duration of reductions that the VIPSC will seek.

The Company believes that any refunds ordered for the period November 1 to December 31, 1987, would not be material to the Company's financial statements. Furthermore, ATN and its attorneys believe that there is a substantial possibility that a VIPSC order reducing

Vitelco' rates by the amount recommended by the VIPSC staff would not be sustained on appeal to the District Court.

During 1987, the VIPSC issued everal orders ordering Vitelco to pay assessments totaling $175,000 to cover certain VIPSC expenses and has petitioned for reconsideration of the VIPSC orders and/or petitioned for appeal to the District Court. Vitelco intends to contest the matter vigorously, and ATN and its attorneys believe that there is a substantial possibility that the District Court will invalidate the VIPSC orders.

No amounts have been accrued for such assessments at December 31, 1987. In February, 1988, Vitelco paid $75,000 under protest and with full reservation of its rights to challenge the lawfulness of the order imposing the assessment.

On March 4, 1988, the VIPSC ordered Vitelco to pay an additional assessment of $75,000. Vitelco has not paid the assessment and intends to contest the matter vigorously, and plans to submit a timely petition for appeal to the District Court. The Company and its attorneys believe that there is a substantial possibility that the District Court will invalidate the VIPSC order.

In October, 1987, Vitelco petitioned for an increase in revenues of approximately $3,500,000 on an annual basis. The VIPSC has docketed the petition, but no hearings have been held to date.

Effective January 1, 1987, the VIPSC detariffed customer premises equipment ("CPE"), and the Company transferred its CPE and the related accumulated depre-

ciation and deferred taxes to investment in nonregulated facilities.

The FCC has adopted a new Uniform System of Accounts ("USOA") effective January 1, 1988. The new USOA requires certain costs, which were previously capitalized, to be expensed. It is anticipated that this change will increase 1988 expenses by approximately $700,000.

(7) RELATED-PARTY TRANSACTIONS:

Under the terms of an agreement between ATN and Vitelco, ATN provides technical, professional and financial advice to Vitelco for a fee equal to 6% of Vitelco's total operating revenue. In addition, the agreement calls for reimbursement to ATN for any salaries and expenses of ATN employees while performing services for Vitelco. Total payments received under this agreement amounted to $1,627,000 in 1987. In Vitelco's last rate case, the VIPSC limited the percentage recoverable by Vitelco in local service revenues for such advisory services to 1% to 1½% of local operating revenues.

In addition, the advisory contract calls for Vitelco to reimburse ATN for salaries and expenses of the Company's employees who perform services directly for Vitelco.

In connection with the acquisition referred to in Note 1, $4,147,000 was paid to affiliated companies of the new stockholders for services rendered in connection with the acquisition. Such amounts are classified in the financial statements as investment in subsidiary ($2,192,000), organization cost ($75,000) and, debt issuance cost ($1,880,000).

During the period from June 25, 1987, to December 29, 1987, the Company entered into a bridge loan of $94,000,000 at a variable interest rate from an affiliate of a stockholder. Vitelco did not guarantee payment of either principal or interest on the bridge loan. Total interest expense reflected in the statement of income includes $6,129,000 applicable to such bridge loans and $235,000 of debt issuance expense related to the bridge loan. The Company believes that $235,000 of debt issuance expense represents a fair allocation of the total costs of acquisition to the bridge loan. The bridge loan was replaced on December 30, 1987, by the permanent financing described in Note 8.

Other than the above, net of amortization, there were no material related-party transactions.

(8) LONG-TERM DEBT:

On December 30, 1987, Vitelco borrowed $60,000,000 from the Rural Telephone Finance Cooperative ("RTFC"). As part of the same transaction, ATN borrowed $44,444,444 from the RTFC. The notes are to be repaid quarterly through December 30, 2002. The notes bear interest at a variable or fixed rate, as provided for in the note, at the lender's option. The interest rate at December 31, 1987, was 7.83%.

The loan and related agreements state that all of the assets of ATN and Vitelco are pledged on both ATN and Vitelco debt. In addition, Vitelco guarantees payment of interest and principal on the loan to ATN. At December 31, 1987, the ability of ATN to service its debt was solely dependent on funds from Vitelco.

The annual requirements for principal payments on long-term debt for the years 1988 through 1992 are as follows:

	Vitelco Amount	ATN Amount
1988	$3,013,408	$ 814,425
1989	3,255,618	880,101
1990	3,518,935	951,063
1991	3,806,665	1,027,738
1992	4,109,170	1,110,615

As a condition of receiving the loan, Vitelco was required to invest $10,444,444 in a subordinated capital certificate with the RTFC. This certificate is noninterest bearing but is entitled to share proportionately in the net earnings of RTFC.

(9) DEFERRED ASSETS:

The debt issuance cost at December 31, 1987, is applicable to the long-term debt and is being amortized on the basis of debt outstanding over the life of the debt.

Organization cost is being amortized over a five-year period beginning at June 25, 1987.